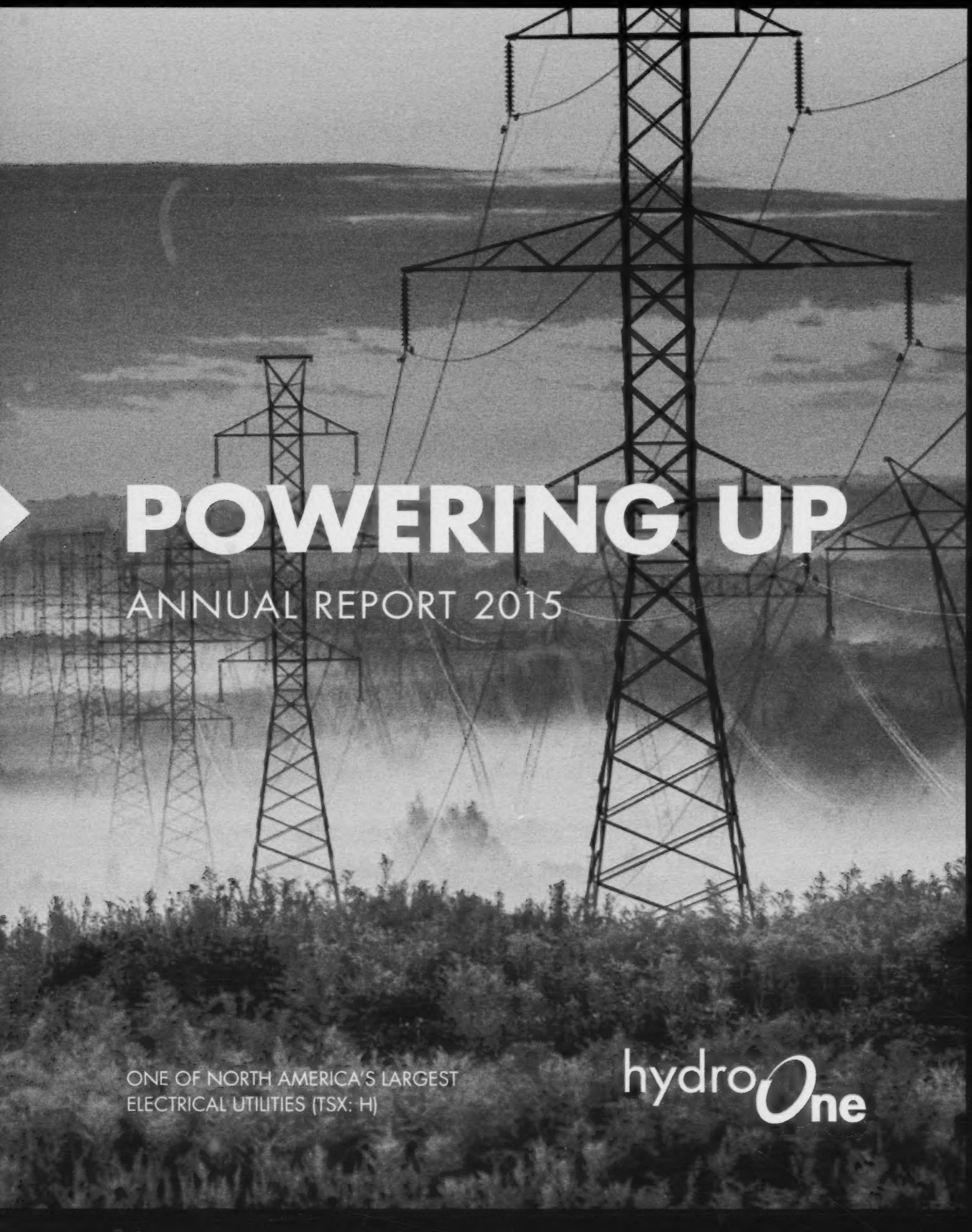
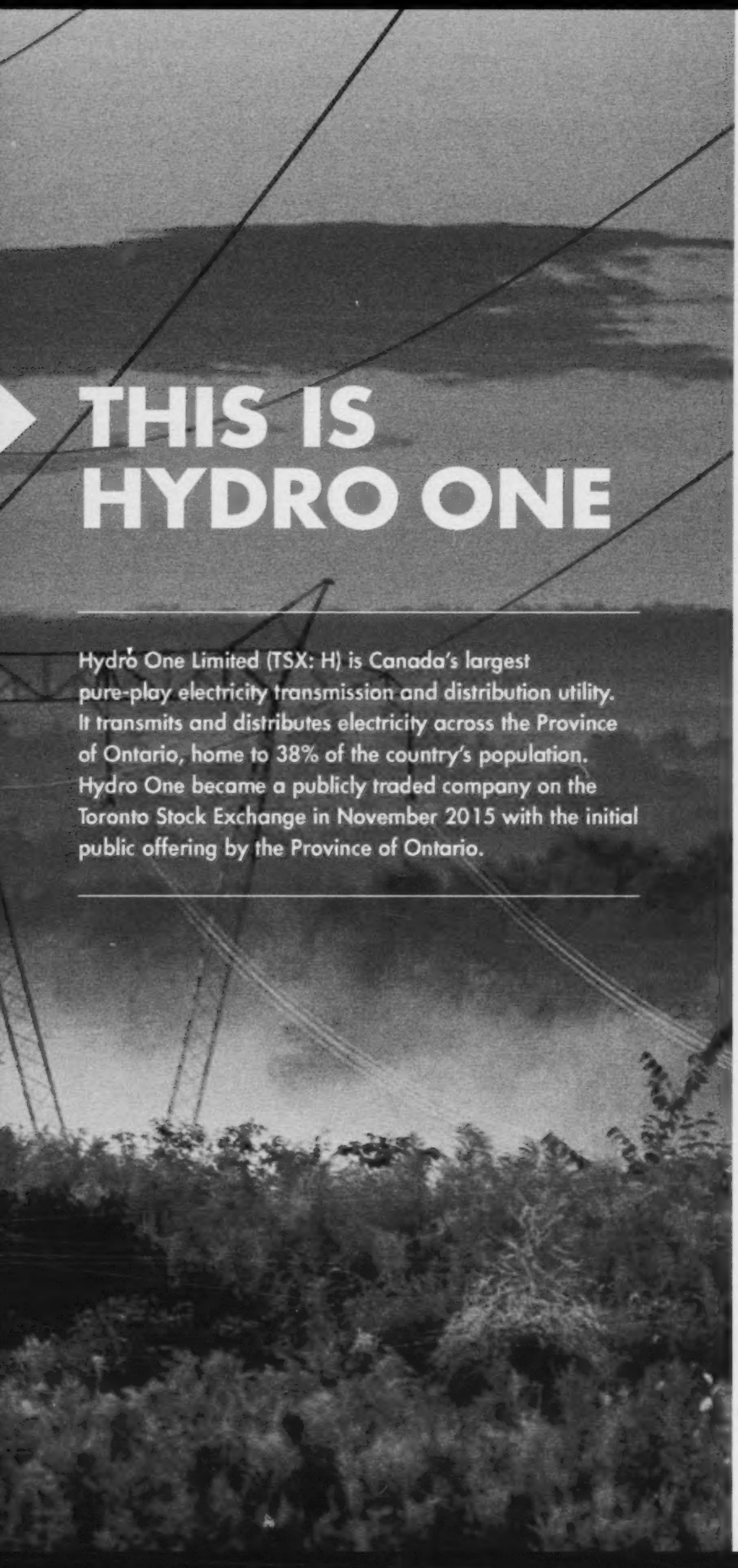


POWERING UP

ANNUAL REPORT 2015

ONE OF NORTH AMERICA'S LARGEST
ELECTRICAL UTILITIES (TSX: H)

hydro One



THIS IS HYDRO ONE

Hydro One Limited (TSX: H) is Canada's largest pure-play electricity transmission and distribution utility. It transmits and distributes electricity across the Province of Ontario, home to 38% of the country's population. Hydro One became a publicly traded company on the Toronto Stock Exchange in November 2015 with the initial public offering by the Province of Ontario.

Hydro One Limited has three reportable segments: the electrical transmission business, the electrical distribution business and a third business segment consisting of the company's telecommunications business and certain corporate activities.

Together, the company's regulated transmission and distribution operations comprise approximately 88% of Hydro One's assets and provide 98% of its net revenues.

Hydro One Telecom leverages the company's telecommunications and tower assets to sell broadband fibre-optic capacity to other carriers, large corporations, government agencies, and healthcare and educational institutions.

A new governance agreement between Hydro One and the Province of Ontario was announced on April 16, 2015. On July 17, 2015 a new independent Board of Directors was appointed to govern Hydro One through its transition into a publicly traded company.

In November 2015, Hydro One Limited completed the initial public offering of 15% of its common shares, with the proceeds of the offering going to the Province of Ontario in the first phase of its previously announced sale of the majority of the company to the public. The common shares are listed and trade on the Toronto Stock Exchange under the symbol "H".

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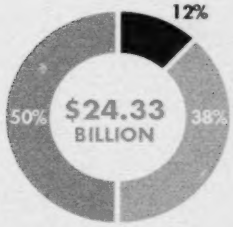
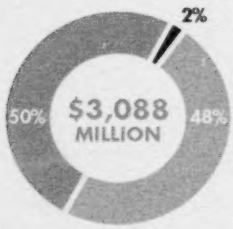
TOTAL ASSETS

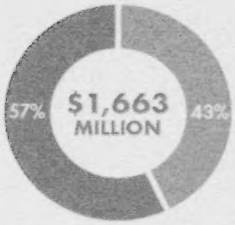


RATE BASE

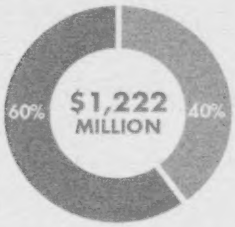
REVENUES (NET OF POWER COSTS)

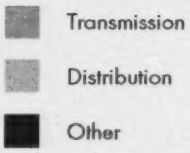


CAPITAL INVESTMENTS



REGULATED EARNINGS BEFORE FINANCING CHARGES AND INCOME TAXES[1]

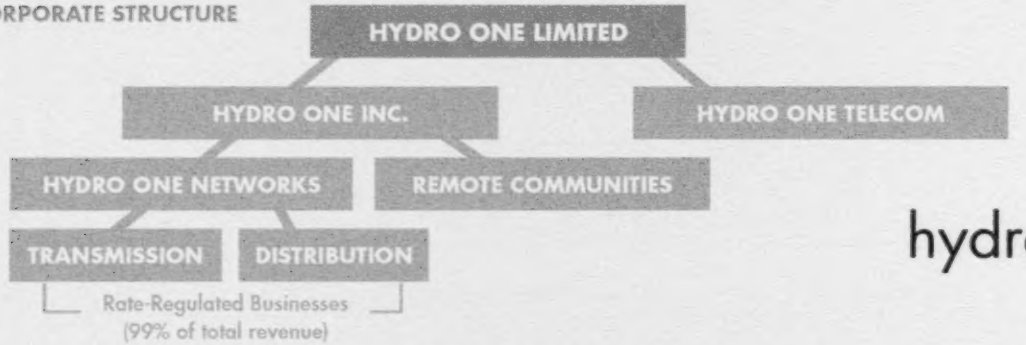




Year ended December 31 *(CAD millions, except as otherwise noted)*	2015	**2014**
Revenues	6,538	6,548
Purchased power	3,450	3,419
Revenues (net of purchased power)	3,088	3,129
Operation, maintenance and administration	1,135	1,192
Depreciation and amortization	759	722
Income before financing charges and income tax expense	1,194	1,215
Financing charges	376	379
Income tax expense	105	89
Net income attributable to common shareholders of Hydro One	690	**731**
Basic and diluted earnings per common share (EPS) *(Canadian dollars)*	1.39	1.53
Adjusted basic and diluted EPS *(Canadian dollars)*[2]	1.16	**1.23**
Net cash from (used in) operating activities	(1,253)	1,256
Adjusted net cash from operating activities[3]	1,557	1,256
Funds from (used in) operations (FFO)	(1,479)	1,293
Adjusted FFO[3]	1,331	1,293
Capital investments	1,663	1,530
Transmission – average monthly Ontario 60-minute peak demand *(MW)*	20,344	20,596
Distribution – electricity distributed to Hydro One customers *(TWh)*	28.9	29.8

[1] Distribution and transmission segments
[2] Calculated using the number of common shares outstanding at December 31, 2015
[3] Excludes $2,810 million impact of deferred income tax asset that resulted as a consequence of leaving the payment in lieu of taxes regime and entering the federal tax regime.

CORPORATE STRUCTURE



hydro One

"Hydro One has a fully independent, diverse and deeply experienced Board of Directors to govern the Company's business, allowing it to execute as an independently controlled and professionally managed commercial entity well positioned to generate growth and value for our shareholders..."

DAVID F. DENISON

Chair of the Board

Dear fellow shareholders,

This was a seminal year of change and movement forward for Hydro One.

The transformative journey began last spring when the Province of Ontario, previously the sole shareholder of Hydro One, made a series of announcements relating to the company, including that it would broaden the ownership through an initial public offering. While the province remains the company's largest shareholder with 84% of the outstanding shares today, it has stated that it intends to make additional tranches of shares available to the public in stages, until it achieves its stated goal of reducing its ownership of Hydro One to 40%.

An integral part of the company's future is a renewed focus on customer service excellence and improved performance. During the past summer, the new Board announced the appointment of Mayo Schmidt as the company's new President and Chief Executive Officer and Michael Vels as its Chief Financial Officer. Both executives have strong track records and demonstrated experience in leading the transformation of large, publicly traded companies into high performance, innovative and customer-focused organizations that enhance customer service, accelerate growth and create significant shareholder value. Together with the technical expertise of the existing Hydro One team, I believe they can help to lead the company forward.

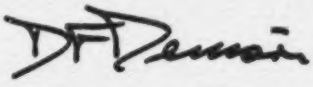
In addition to rolling up their sleeves in their critical new roles, the Hydro One management team led one of the largest and most successful initial public offerings in Canada in more than 15 years. The shares of Hydro One began trading on the Toronto Stock Exchange on November 5th.

To facilitate the change in ownership structure associated with the initial public offering, the province announced a new governance agreement between Hydro One and the province. This agreement ensures that the company is governed as an independent commercial entity going forward, providing confidence that the province is strictly playing the role of shareholder and not manager. Over the ensuing months, the new Board was assembled, drawing upon a diverse and accomplished group of proven leaders to govern Hydro One's transformation with a renewed focus on customer service excellence and improved performance and reliability. My fellow Board members were selected for their independence, commercial experience and strong governance expertise concerning public companies, customer service, the electricity sector and public policy.

As management and the Board work together to put in place a broad strategy to take Hydro One forward, work has already commenced across the company to strengthen customer service and performance excellence while putting in place initiatives to accelerate growth.

I would like to recognize the important foundational work of the previous Chair, Sandra Pupatello, and her Board, and acknowledge the efforts of former President and Chief Executive Officer Carmine Marcello: his contribution and leadership was essential to Hydro One's successful transition in 2015. Finally, I would like to thank the more than 5,500 Hydro One employees who work tirelessly – often around the clock and in hazardous weather and conditions – to ensure that electricity is delivered safely, reliably and cost-effectively to the millions of citizens of Ontario. It is their efforts and commitment that enable this great company to deliver for you – our shareholders, our customers and our communities – and we look forward to taking your company even further in 2016.

Thank you for your support,



David F. Denison, OC

Chair of the Board
Hydro One Limited

"2015 was a year of tremendous positive change for Hydro One. The team is intently focused on transforming this significant North American electrical utility into a high-performance commercial organization with considerable muscle to accelerate growth and consistently deliver on its promises..."

MAYO SCHMIDT

President and CEO

Dear fellow shareholders,

It is clear that 2015 was a pivotal year for your company as Hydro One charted a new course towards becoming a publicly traded, increasingly customer-focused and performance-driven company that offers dependable dividends and robust, predictable growth prospects.

It was a year of tremendous positive change that opened the door to a very bright future.

The size, strength and efficiency of our electrical grid is critical to reliably delivering the electricity that sustains and secures the economic and social well-being of every community in Ontario. This past year, the company made important investments to modernize and bolster the grid, investing approximately $1.7 billion in capital projects across both our transmission and distribution networks. Over the next few years, we will invest in significant infrastructure that is needed to maintain and modernize the critical electrical systems that we all depend on. We are stewards of this system, a mission we take very seriously.

Hydro One is embarking on a journey to take a leadership position in the North American utility landscape. Through building on our strong foundation, we have the opportunity to become a leader in this dynamic and evolving environment. To enable this, we have undertaken a strategic planning process to define our future.

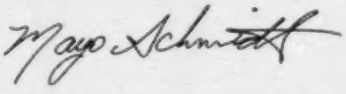
We know that we need to understand the needs of our customers and stakeholders, including First Nations and Métis communities. Serving these needs effectively and efficiently will drive our business decisions. Our strategy will ensure we are ready to adapt to the emerging technology landscape and position our business for success. We will build world-class competencies and position ourselves to grow in the long term.

Hydro One is fortunate to operate in a stable and supportive regulatory environment with a transparent and predictable rate-setting process. The company plays an essential leadership role in the Ontario electricity industry.

We are focused on making life better for our customers. We improve their lives by treating them with respect, by making certain our system is reliable and ready for the future, by managing our costs and thus the cost of our service, and by having highly trained men and women across Ontario who are ready to respond 24/7 when storms and extreme weather disrupt service.

I believe we are uniquely positioned to make the most of the significant opportunities that lie ahead – and transform our business into a great Canadian company that stands out for its commitment to its customers and its performance for its shareholders.

On behalf of our 5,500 employees, thank you for your investment and interest in our progress. I would like to thank the Board of Directors for its support and its confidence in management. I would also like to thank employees across Ontario for embracing Hydro One's transformation and for their unwavering commitment to our customers. The future is bright.



Mayo Schmidt
President and CEO
Hydro One Limited

ELECTRICAL TRANSMISSION OPERATIONS

Hydro One's electrical transmission system totals approximately 29,000 circuit kilometres of high-voltage lines, towers and transformers, operating at 500 kV, 230 kV or 115 kV. Hydro One's grid transmits electricity from hydroelectric, nuclear, gas, wind and solar power generation sources to customers across Ontario, including 47 local distribution companies (LDCs), Hydro One's own local distribution systems and 90 large industrial customers directly connected to the transmission system.

The transmission operations service approximately 96% of the Province of Ontario by capacity and represent approximately 50% of the total assets and provide 50% of the net revenues of the company.

The transmission system is linked to five jurisdictions adjacent to Ontario (Manitoba, Minnesota, Michigan, New York and Quebec) through high-voltage interconnections. The transmission operations are regulated by the Ontario Energy Board (OEB) and the National Energy Board (NEB), together with an operating agreement with the Independent Electricity System Operator (IESO) and the North American Electric Reliability Corporation (NERC). Hydro One is also a partner in the Bruce to Milton Limited Partnership, which is a unique partnership between the company and the Saugeen Ojibway Nation Finance Corporation, operating a 176-kilometre long dual circuit transmission line between the Bruce Nuclear Generating Station and Hydro One's Milton Switching Station.

Our transmission assets can be divided into four functional categories:

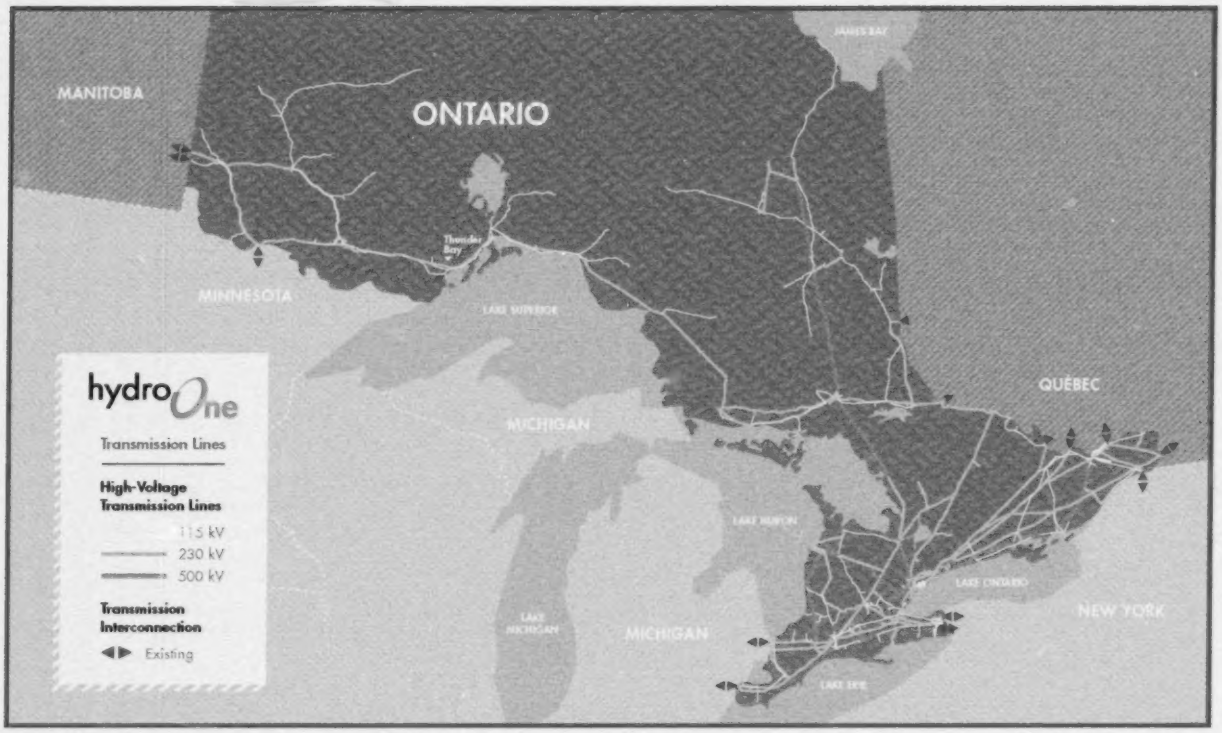
1. **Transmission stations:** These facilities are used for the delivery of power, voltage transformation and switching, and serve as connection points for both customers and generators.
2. **Transmission lines:** Bulk transmission lines are main lines delivering power from generating stations or connections to receiving terminal stations. Area supply lines take power from the network and transmit it to customer supply transmission stations at customer load centres.
3. **Network operations:** All transmission assets and many sub-transmission assets are managed from one central location, the Ontario Grid Control Centre.
4. **Telecommunications facilities:** These facilities ensure the company's telecommunications requirements are met, with respect to the protection and operation of the power system as well as voice and administrative data. Our subsidiary Hydro One Telecom sells excess capacity on our fibre-optic network.

TRANSMISSION STATIONS

292

CIRCUIT KILOMETRES OF HIGH-VOLTAGE LINES

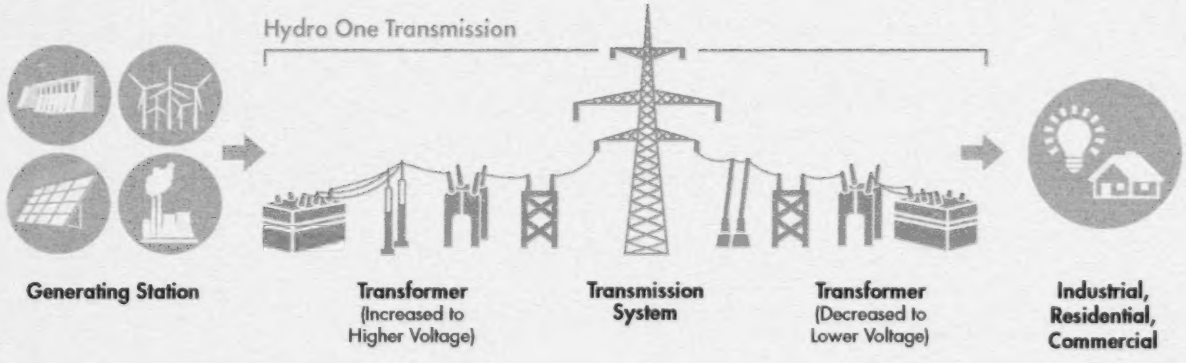
29,000



	TRANSMISSION SEGMENT
Customers	47 local distribution companies and 90 large industrial customers connected directly to the transmission network
Assets	292 transmission stations and approximately 29,000 circuit kilometres of high-voltage lines
Current Rate Base	$10.18 billion[1]
Allowed ROE (2016)	9.19%

[1] *Current transmission rate base as at December 31, 2015 includes 100% of B2MLP rate base.*

ONTARIO'S ELECTRICITY SYSTEM



ELECTRICAL DISTRIBUTION OPERATIONS

Hydro One's electrical distribution system totals approximately 123,000 circuit kilometres of lower-voltage power lines, poles and transformers, serving more than 1.3 million customers across Ontario.

As Hydro One operates in both rural and urban centres across Ontario, customers benefit from our integrated planning and the coordinated operations of our distribution and transmission systems and workforce.

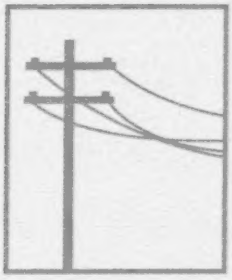
In June 2015, Hydro One announced the closing of its acquisition of Haldimand County Utilities, adding 21,200 customers to its local distribution network. In October, the closing of the acquisition of Woodstock Hydro Holdings Inc., including its wholly-owned subsidiary Woodstock Hydro Services Inc., added 15,800 customers, to be integrated with Hydro One's network in 2016.

Hydro One Remote Communities Inc. operates and maintains the generation and distribution assets used to supply electricity to 21 remote communities across northern Ontario that are not connected to the electricity transmission grid.

HYDRO ONE HAS A LARGELY RURAL AND SUBURBAN FOOTPRINT

1.3 MILLION CUSTOMERS

1.6 MILLION POLES

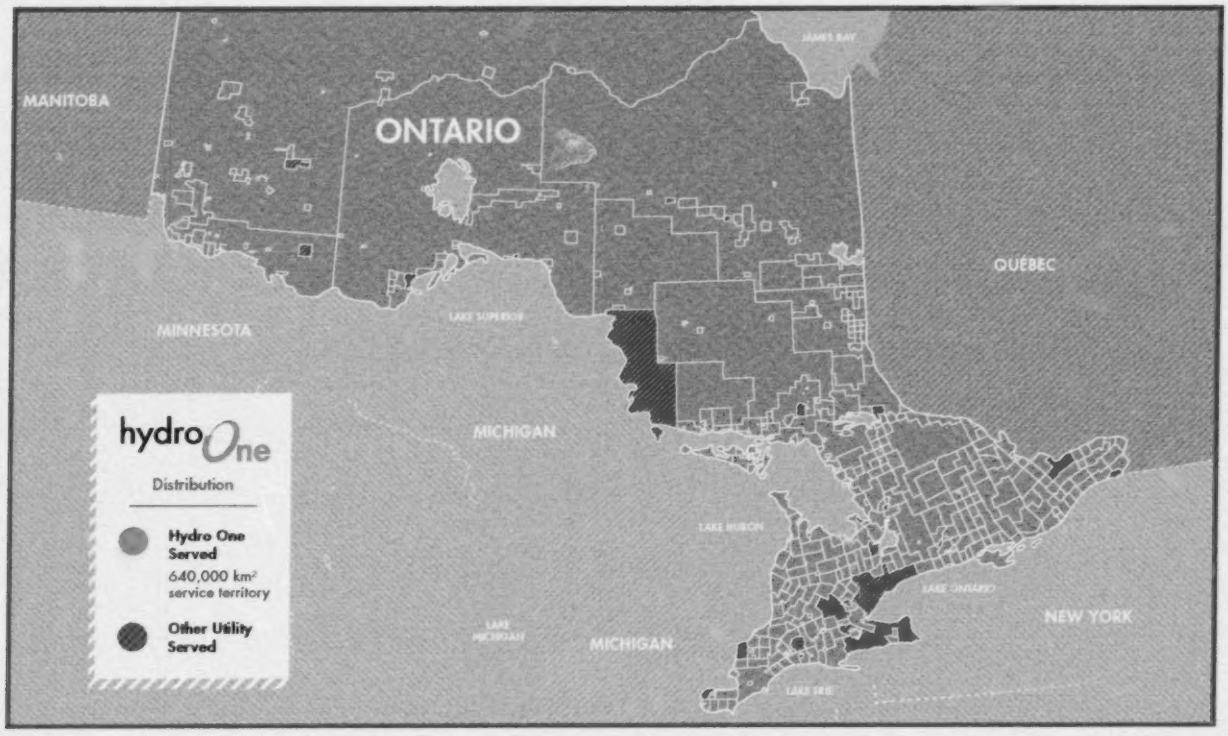


CIRCUIT KILOMETRES OF LOWER-VOLTAGE LINES

123,000

DISTRIBUTION AND REGULATION STATIONS

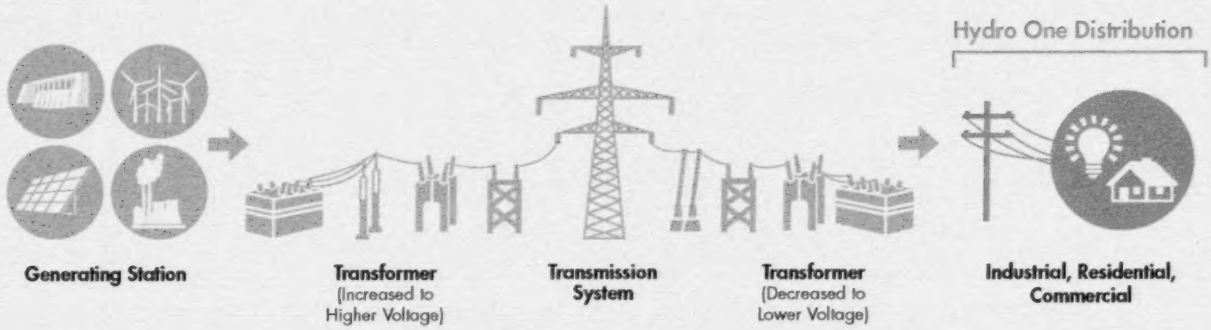
c. 1,000



	DISTRIBUTION SEGMENT
Customers	Approximately 1.3 million residential and business customers located mostly in rural areas, covering approximately 75% of the geographic area of the province, equal to roughly 640,000 square kilometres
Assets	123,000 circuit kilometres of lower-voltage distribution lines and approximately 1,000 distribution and regulating stations
Current Rate Base	$6.74 billion[1]
Allowed ROE (2016)	9.19%

[1] *Current distribution rate base as at December 31, 2015.*

ONTARIO'S ELECTRICITY SYSTEM



SERVING CUSTOMERS

Throughout 2015, Hydro One continued to put customers at the core of its decision-making, planning and execution. Every day the organization is focused on exceeding customer expectations. Whether it's launching new customer-friendly tools or mobilizing hundreds of employees to restore power, Hydro One's future path to success lies with our ability to exceed expectations.

CUSTOMER COMMITMENTS

In 2015, Hydro One was the first utility in Canada to launch Customer Commitments and service level guarantees. Developed with input from more than 40,000 customers and the company's Customer Service Advisory Panel, these five commitments provide assurance to customers about the service they can expect from Hydro One:

1. **We will provide you with a bill you can trust and understand.**
2. **We will provide you with a reliable supply of electricity.**
3. **We will make it easy to do business with us.**
4. **We will courteously and promptly work to resolve any issues you may have.**
5. **We will help you manage your electricity use.**

MOBILE OUTAGE APP

Customer service includes keeping customers connected to the information that is most important to them. The company's mobile outage app – available free to customers on their smartphones – was downloaded more than 60,000 times during 2015, totaling more than 286,000 since its launch in May 2012.

OUTAGE ALERTS

Drawing on the success of the mobile app, Hydro One was the first utility in Canada to launch personalized text and email alerts to customers, proactively informing them of outages that might affect their homes, cottages, farms or small businesses. Customers who register for this service receive alerts and updates on estimated times of restoration when an outage has been reported near their residences. Customers decide when and how they receive messages. To date, more than 7,000 customers have signed up for the service.

OFFICE OF THE OMBUDSMAN

To further support customer service, in October the company's Board of Directors appointed Fiona Crean to the role of Ombudsman for Hydro One. Having most recently served as the City of Toronto's ombudsman, Ms. Crean has worked in the area of complaints investigation and dispute resolution for more than 25 years.

STORM RESPONSE

Wind, snow and rain are a reality of life in Ontario. Across the province, the men and women of Hydro One are available 24 hours a day, seven days a week, to restore power for customers if the lights go out.

From the state-of-the-art Ontario Grid Control Centre, highly trained employees monitor all potential events, including weather, solar storms and geomagnetic disturbances that could affect Hydro One's system. The centre provides Hydro One with the industry-leading ability to remotely monitor and operate transmission equipment, respond to alarms and restore or reroute interrupted power.

When an alert is issued, the entire organization begins mobilizing staff and equipment to ensure power is restored as efficiently as possible. This means moving crews and equipment to where they are needed to make sure that power can be restored safely and quickly. With a workforce trained to the highest standards, crews can travel more than 500 kilometres to aid in restoration.

Working through holidays, in the harshest of conditions and in remote areas of the province, Hydro One employees not only restore power, but restore life back to normal for customers.

SAFETY, COMMUNITY AND THE ENVIRONMENT

SAFETY

The safety of the public, the communities Hydro One serves and the people of Ontario is every employee's responsibility.

From proper job planning to a trained and highly-skilled workforce, Hydro One emphasizes the importance of a safe workplace across every line of business. The result of this focus was seen in 2015 as Hydro One achieved its ambitious health and safety target, recording only 1.68 incidents per 200,000 hours worked.

Hydro One was awarded the Electrical Safety Authority's Powerline Safety Award for its community outreach with the company's mobile Electricity Discovery Centre. More than 30,000 visitors from 26 communities learned about electrical safety, how to conserve energy and the role Hydro One plays in the community.

COMMUNITY

Hydro One believes in the importance of connecting with the communities where we live and work through sponsorships, donations, scholarship programs and volunteering. These charitable giving programs broadly support safety and injury prevention, education and community support. They are an important link to the hundreds of communities that the company serves across the province.

Community Investment

Furthering the company's commitment to First Nations and Métis communities, in February 2015 Hydro One announced a three-year funding extension for Right to Play's Promoting Life-skills in Aboriginal Youth program. Hydro One is investing $100,000 each year to support after-school programming, sport for developmental activities, youth leadership, and health and wellness education.

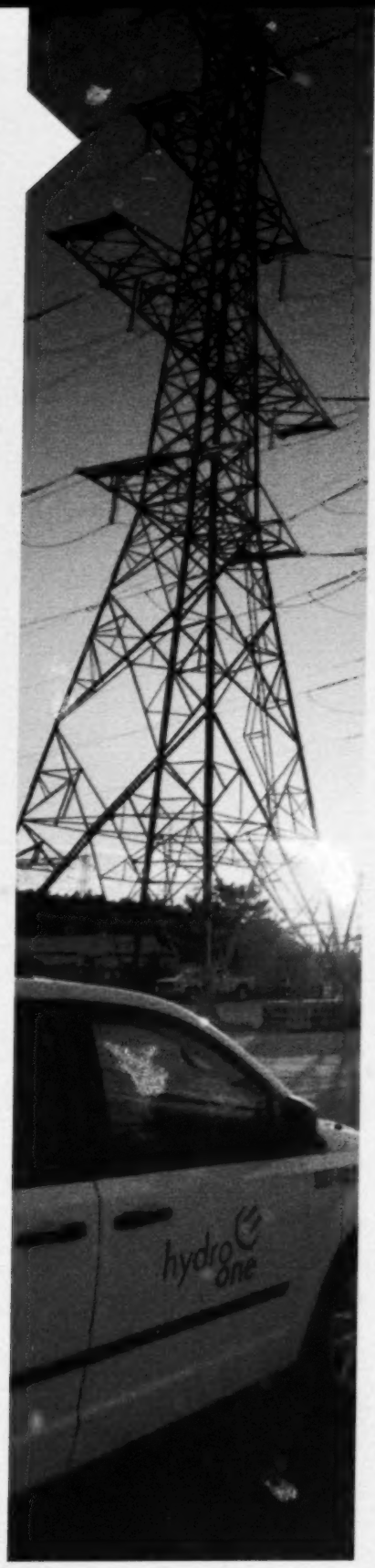
Scholarship Programs

In 2015, 13 female engineering students received Hydro One's Women in Engineering Scholarship for their outstanding achievements in electrical engineering. Winners receive a financial award along with a paid opportunity to work for Hydro One in a developmental student work placement. In celebration of National Aboriginal Day, in June Hydro One awarded 12 students with the Leonard S. (Tony) Mandamin Scholarship, which is granted annually to First Nations, Métis or Inuit post-secondary students.

CORPORATE SOCIAL RESPONSIBILITY

In January, Hydro One was designated as a Sustainable Electricity Company by the Canadian Electricity Association (CEA). This designation established by the CEA for utilities across Canada recognizes success building on the three foundational pillars of sustainability – environmental, social, and economic performance. It requires utilities to establish an Environmental Management System consistent with the ISO 14001 standard; to take the actions and meet the expectations laid out in the ISO 26000 Guidance on Social Responsibility. Hydro One is only the fourth electric utility in Canada to receive this designation.

For further information on Hydro One's commitments to customers, safety, communities and the environment, please go to: www.HydroOne.com/OurCommitment.



CORPORATE GOVERNANCE OVERVIEW

Hydro One and the Board recognize the importance of corporate governance to the effective management of the company. Independence, integrity and accountability are the foundation of the company's approach to corporate governance. It is in the long-term best interests of our shareholders as well as our customers and promotes and strengthens relationships with employees, the communities in which the company operates and other stakeholders of the company.

Hydro One's Board of Directors was appointed on July 17, 2015, drawing upon a diverse and accomplished group of proven business leaders with deep corporate governance experience. The Board's primary role is overseeing corporate performance and the quality, depth and continuity of management required to meet the company's strategic objectives.

Hydro One is committed to best practices that will allow us to honour important fiduciary and oversight responsibilities. The Board regularly reviews and revises the company's governance practices in response to changing governance expectations and regulations. Our practices meet the rules and regulations issued by Canadian Securities Administrators and the Toronto Stock Exchange, including national corporate governance guidelines and related disclosure requirements.

The Audit Committee reviews the integrity of the company's financial statements and financial reporting process, internal control over financial reporting, enterprise risk management, disclosure controls and procedures, and compliance with other related legal and regulatory requirements. The committee also assists the Board in fulfilling its oversight responsibilities with respect to financial reporting, including overseeing the independence, qualifications and appointment of external auditors as well as the performance of the company's finance function, auditors (both external and internal) and the auditing, accounting and financial reporting process.

The Nominating, Corporate Governance, Public Policy and Regulatory Committee manages and oversees the process of nominating new directors to the Board in accordance with the governance agreement between the company and the Province of Ontario. The committee makes recommendations respecting the Board's approach to corporate governance, overseeing director orientation, education, performance evaluation, compensation and protection. The committee also oversees the company's relationship with shareholders, communities, stakeholders, electricity regulators, customers, the Province of Ontario and the company's approach to corporate social responsibility, including its sponsorship and donation programs.

The Human Resources Committee assists the Board in discharging the Board's oversight responsibilities relating to compensation, attraction and retention of key senior management, employee benefits, labour relations and succession planning.

The Health, Safety, Environment and First Nations and Métis Committee is responsible for oversight relating to effective occupational health and safety and environmental policies and practices at the company as well as the company's relationships with First Nations and Métis communities.

For a complete description of Hydro One's corporate governance structure and practices and individual director biographical information, please go to: www.HydroOne.com/Investors.

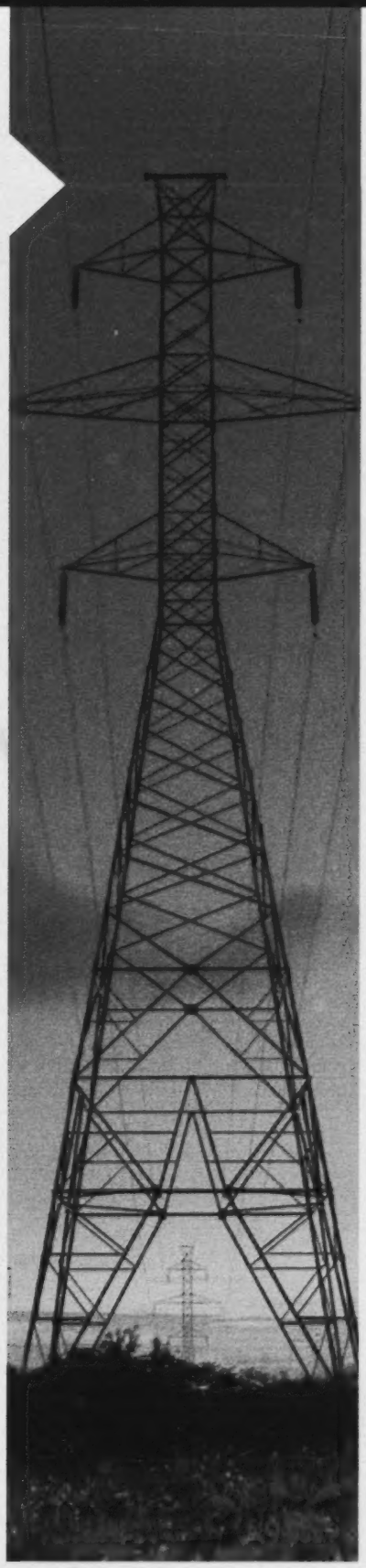
BOARD OF DIRECTORS AND COMMITTEES

★ = CHAIR
▲ = MEMBER

	AUDIT	NOMINATING, CORPORATE GOVERNANCE, PUBLIC POLICY AND REGULATORY	HUMAN RESOURCES	HEALTH, SAFETY, ENVIRONMENT AND FIRST NATIONS AND MÉTIS
David Denison (Chair)				
Mayo Schmidt (President and CEO)				
Ian Bourne		▲	★	
Charles Brindamour	▲		▲	
Marc Caira		▲	▲	
Christie Clark		▲	▲	
George Cooke	▲			▲
Marianne Harris			▲	★
Jim Hinds	▲			▲
Kathryn Jackson		▲		▲
Roberta Jamieson	▲			▲
Frances Lankin	▲	▲		
Philip Orsino	★	▲		
Jane Peverett		★	▲	
Gale Rubenstein			▲	▲

HYDRO ONE GOOD GOVERNANCE PRACTICES

100% Director Independence	Code of Business Conduct and Whistleblower Hotline	Annual Reviews of Board and Committee Performance
Board Education Sessions	Committee Authority to Retain Independent Advisors	Board and Committee In-Camera Discussions
Term Limits for Directors	Director Share Ownership Guidelines	Commitment to Director Diversity



WHY INVEST IN HYDRO ONE?

Opportunities to transition to a customer focused performance culture under Ontario's emerging incentive-based regulation

One of the largest electrical utilities in North America, with significant scale and a leadership position in Canada's most populated province

One of the strongest investment grade balance sheets in the utility sector

Unique combination of electrical transmission and local distribution, with no power generation assets or material exposure to commodity prices

Attractive dividend yield with 70 – 80% target payout ratio and opportunity for growth with rate base expansion

The business operates in a stable, transparent and collaborative rate-regulated environment

2015 IPO was the first phase of the largest-ever privatization by the Province of Ontario providing opportunities for public participation in asset transformation

Predictable growth profile, with consistent rate base growth expected under multi-year approved capital investment program to upgrade aging infrastructure

Strong governance structure and a fully independent Board allow the company to operate autonomously, transform its culture and drive shareholder value creation on multiple fronts

Proven management with demonstrated experience transforming organizations, accelerating performance and creating significant shareholder value

A unique opportunity to participate in the transformation of a premium, large-scale utility

hydro One

Management's Discussion and Analysis

For the years ended December 31, 2015 and 2014

The following Management's Discussion and Analysis (MD&A) of the financial condition and results of operations should be read together with the consolidated financial statements and accompanying notes (the Consolidated Financial Statements) of Hydro One Limited (Hydro One or the Company) for the year ended December 31, 2015. The Consolidated Financial Statements are presented in Canadian dollars and have been prepared in accordance with United States (US) Generally Accepted Accounting Principles (GAAP). All financial information in this MD&A is presented in Canadian dollars, unless otherwise indicated.

The Company has prepared this MD&A in accordance with National Instrument 51-102 – Continuous Disclosure Obligations of the Canadian Securities Administrators. This MD&A provides information for the year ended December 31, 2015, based on information available to management as of February 11, 2016.

Initial Public Offering

In November 2015, Hydro One and the Province of Ontario (Province) completed an initial public offering (IPO) on the Toronto Stock Exchange of 15% of the Company's 595 million outstanding common shares. Prior to the completion of the IPO, Hydro One and its subsidiary, Hydro One Inc., completed a series of transactions (Pre-Closing Transactions) that resulted in, among other things, the acquisition by Hydro One of all of the issued and outstanding shares of Hydro One Inc. from the Province and the issuance of new common shares and preferred shares of Hydro One to the Province. Both Hydro One and Hydro One Inc. are reporting issuers. See section "Other Developments – Change in Hydro One Ownership Structure" for details relating to the IPO.

Current year information consists of the results of Hydro One Inc. up to October 31, 2015, and the consolidated results of Hydro One and Hydro One Inc. from November 1, 2015 to December 31, 2015. The comparative information consists of the results of Hydro One Inc. as at and for the year ended December 31, 2014.

Consolidated Financial Highlights And Statistics

Year ended December 31

(millions of Canadian dollars, except as otherwise noted)	2015	2014	Change
Revenues	6,538	6,548	(0.2%)
Purchased power	3,450	3,419	0.9%
Revenues, net of purchased power	3,088	3,129	(1.3%)
Operation, maintenance and administration costs	1,135	1,192	(4.8%)
Depreciation and amortization	759	722	5.1%
Financing charges	376	379	(0.8%)
Income tax expense	105	89	18.0%
Net income attributable to common shareholders of Hydro One	690	731	(5.6%)
Basic and diluted earnings per common share (EPS)	$1.39	$1.53	(9.2%)
Pro forma adjusted non-GAAP basic and diluted EPS[1]	$1.16	$1.23	(5.6%)
Net cash from (used in) operating activities	(1,253)	1,256	(199.8%)
Adjusted net cash from operating activities[1]	1,557	1,256	24.0%
Funds from (used in) operations (FFO)[1]	(1,479)	1,293	(214.4%)
Adjusted FFO[1]	1,331	1,293	2.9%
Capital investments	1,663	1,530	8.7%
Transmission: Average monthly Ontario 60-minute peak demand *(MW)*	20,344	20,596	(1.2%)
Distribution: Units distributed to Hydro One customers *(TWh)*	28.9	29.8	(3.0%)
Debt to capitalization ratio[2]	50.7%	52.8%	

[1] See section "Non-GAAP Measures" for description and reconciliation of pro forma adjusted non-GAAP basic and diluted EPS, adjusted net cash from operating activities, FFO and adjusted FFO.

[2] Debt to capitalization ratio has been calculated as total debt (includes total long-term debt and short-term borrowings, net of cash) divided by total debt plus total shareholder's equity, including preferred shares but excluding any amounts related to non-controlling interest.

Overview

Hydro One is the largest electricity transmission and distribution company in Ontario. Through its subsidiary, Hydro One Inc., Hydro One owns and operates substantially all of Ontario's electricity transmission network, and is the largest electricity distributor in Ontario. Hydro One has three business segments: (i) Transmission Business; (ii) Distribution Business; and (iii) Other Business (telecommunications).

Transmission Business

Hydro One's transmission business owns, operates and maintains Hydro One's transmission system, which accounts for approximately 96% of Ontario's transmission capacity. The Transmission Business consists of the transmission system operated by Hydro One Inc.'s subsidiary, Hydro One Networks Inc. (Hydro One Networks), and a 66% interest in B2M Limited Partnership (B2M LP), a limited partnership between Hydro One and the Saugeen Ojibway Nation in respect of the Bruce-to-Milton transmission line. The Company's Transmission Business is a rate-regulated business that earns revenues mainly from charging transmission rates that are approved by the Ontario Energy Board (OEB). The Transmission Business represented approximately 50% of the Company's total assets as at December 31, 2015, and approximately 50% of its total revenues, net of purchased power, in 2015.

	2015	2014
Electricity transmitted *(TWh)*	**137.0**	139.8
Transmission lines spanning the province *(circuit-kilometres)*	**29,355**	29,344
Rate base *(millions of Canadian dollars)*	**10,175**	9,934
Capital investments *(millions of Canadian dollars)*	**943**	845

Note: TWh means terawatt-hours.

Distribution Business

Hydro One's Distribution Business is the largest in Ontario and consists of the distribution system operated by Hydro One Inc.'s subsidiaries Hydro One Networks and Hydro One Remote Communities Inc. The Company's Distribution Business is a rate-regulated business that earns revenues mainly by charging distribution rates that must be approved by the OEB. The Distribution Business represented approximately 38% of the Company's total assets as at December 31, 2015, and approximately 48% of its total revenues, net of purchased power, in 2015.

	2015	2014
Electricity distributed to Hydro One customers *(TWh)*	**28.9**	29.8
Electricity distributed through Hydro One lines *(TWh)*[1]	**40.7**	42.4
Distribution lines spanning the province *(circuit-kilometres)*	**123,425**	123,657
Distribution customers *(number of customers)*	**1,347,231**	1,439,321
Rate base *(millions of Canadian dollars)*	**6,739**	6,415
Capital investments *(millions of Canadian dollars)*	**711**	680

[1] Units distributed through Hydro One lines represent total distribution system requirements and include electricity distributed to consumers who purchased power directly from the Independent Electricity System Operator (IESO).

Other Business

Hydro One's Other Business segment consists of the Company's telecommunications business and certain corporate activities. The telecommunications business provides telecommunications support for the Company's Transmission and Distribution Businesses, and also offers communications and IT solutions to organizations with broadband network requirements utilizing Hydro One Telecom Inc.'s (Hydro One Telecom) fibre optic network to provide diverse, secure and highly reliable connectivity. Hydro One's other business segment is not rate-regulated. This segment represented approximately 12% of Hydro One's total assets as at December 31, 2015, and approximately 2% of its total revenues, net of purchased power, in 2015.

Primary Factors Affecting Results Of Operations

Transmission Revenues

Transmission revenues primarily consist of the Company's transmission rates approved by the OEB which are charged based on the monthly peak electricity demand across Hydro One's high-voltage network. Transmission rates are designed to generate revenues necessary to construct, upgrade, extend and support a transmission system with sufficient capacity to accommodate maximum forecasted demand and a regulated return on the Company's investment. Peak electricity demand is primarily influenced by weather and economic conditions. Transmission revenues also include export revenues associated with transmitting electricity to markets outside of Ontario. Ancillary revenues include revenues from providing maintenance services to generators and from third-party land use.

Distribution Revenues

Distribution revenues include the distribution rates approved by the OEB and amounts to recover the cost of purchased power used by the customers of the distribution business. Distribution rates are designed to generate revenues necessary to construct and support local distribution system with sufficient capacity to accommodate existing and new customer demand and a regulated return on the Company's investment. Accordingly, distribution revenues are influenced by distribution rates, the cost of purchased power, and the amount of electricity the Company distributes. Distribution revenues also include ancillary distribution service revenues, such as fees related to the joint use of Hydro One's distribution poles by the telecommunications and cable television industries, as well as miscellaneous charges such as charges for late payments.

Purchased Power Costs

Purchased power costs are incurred by the distribution business and represent the cost of purchased electricity delivered to customers within Hydro One's distribution service territory. These costs comprise the wholesale commodity cost of energy, in addition to wholesale market service and transmission charges levied by the Independent Electricity System Operator (IESO). Hydro One passes the cost of electricity that it delivers to its customers, and is therefore not exposed to wholesale electricity commodity price risk.

Operation, Maintenance and Administration Costs

Operation, maintenance and administration (OM&A) costs are incurred to support the operation and maintenance of the transmission and distribution systems, and other costs such as property taxes related to transmission and distribution lines, stations and buildings.

Transmission OM&A costs are incurred to sustain the Company's high-voltage transmission stations, lines and rights-of-way, and include preventive and corrective maintenance costs related to power equipment, overhead transmission lines, transmission station sites, and forestry control to maintain safe distance between line spans and trees. Distribution OM&A costs are required to maintain the Company's low-voltage distribution system, and include costs related to distribution line clearing and forestry control to reduce power outages caused by trees, line maintenance and repair, as well as land assessment and remediation. Hydro One manages its costs through ongoing efficiency and productivity initiatives, while continuing to complete planned work programs associated with the development and maintenance of its transmission and distribution networks.

Depreciation and Amortization

Depreciation and amortization costs relate primarily to depreciation of the Company's property, plant and equipment, and amortization of certain intangible assets and regulatory assets. Depreciation expense also includes the costs incurred to remove property, plant and equipment where no asset retirement obligations have been recorded on the balance sheet.

Financing Charges

Financing charges relate to the Company's financing activities, and include interest expense on the Company's long-term debt, gains and losses on interest rate swap agreements, net of interest earned on short-term and long-term investments. A portion of financing charges incurred by the Company is capitalized to the cost of property, plant and equipment associated with the periods during which such assets are under construction before being placed in-service.

Income Taxes

Hydro One and its subsidiaries were exempt from regular Canadian federal and Ontario income tax (Federal Tax Regime) and instead paid an equivalent amount referred to as payments in lieu of corporate income taxes (PILs) to the Ontario Electricity Financial Corporation (OEFC) under the *Electricity Act* (PILs Regime) until October 2015. Since then, Hydro One and its subsidiaries have been subject to the Federal Tax Regime. See further details in section "Other Developments – PILs Deemed Disposition Rules."

Results of Operations

Net Income

Net income attributable to common shareholders for the year ended December 31, 2015 of $690 million is a decrease of $41 million or 5.6% from the prior year. Significant influences on net income included:

- milder weather in 2015 resulted in a decrease in transmission revenues, mainly due to lower average Ontario peak demand in 2015 compared to 2014, particularly in June, November, and December;
- the effective income tax rate of 12.8% in 2015 compared to an effective tax rate of 10.6% in 2014;
- OM&A costs were lower than the prior year due to:
  - lower costs related to remediating the Company's customer information system, lower customer support expenses and lower bad debt expenses; and
  - lower preventative maintenance related to vegetation management; partially offset by
  - in 2014, insurance proceeds related to 2013 floods at the Company's Richview and Manby transformer stations were recorded as a reduction in 2014 OM&A costs and did not recur in 2015; and
  - during 2015, the Company recorded expenditures related to the integration of acquired local distribution companies.

Revenues

Year ended December 31

(millions of Canadian dollars, except as otherwise noted)	2015	2014	Change
Transmission	1,536	1,588	(3.3%)
Distribution	4,949	4,903	0.9%
Other	53	57	(7.0%)
	6,538	6,548	(0.2%)
Transmission: Average monthly Ontario 60-minute peak demand *(MW)*	20,344	20,596	(1.2%)
Distribution: Units distributed to Hydro One customers *(TWh)*	28.9	29.8	(3.0%)

Transmission Revenues

The decrease of $52 million or 3.3% in transmission revenues for the year ended December 31, 2015 was primarily due to lower average monthly Ontario 60-minute peak demand due to industrial customers shifting energy use away from system-wide peaks in the winter months of 2015 and generally milder weather in 2015, which more than offset increased transmission rates for 2015.

Distribution Revenues

The increase of $46 million or 0.9% in distribution revenues for the year ended December 31, 2015 was primarily due to higher OEB-approved distribution rates and higher purchased power costs, partially offset by decreased revenues due to the spin-off of Hydro One Inc.'s subsidiary, Hydro One Brampton Networks Inc. (Hydro One Brampton).

Operation, Maintenance and Administration Costs

Year ended December 31

(millions of Canadian dollars)	2015	2014	Change
Transmission	426	394	8.1%
Distribution	633	742	(14.7%)
Other	76	56	35.7%
	1,135	1,192	4.8%

Transmission OM&A Costs

The increase of $32 million or 8.1% in transmission OM&A costs for the year ended December 31, 2015 was primarily due to the following:

- expenses related to write-offs of project and inventory costs due to revisions of asset replacement strategies;
- higher expenditures during 2015 related to work required to adhere to the North American Electric Reliability Corporation (NERC) Critical Infrastructure Protection (Cyber Security) standards; and

- in 2014, insurance proceeds related to 2013 floods at the Company's Richview and Manby transformer stations were recorded as a reduction in 2014 OM&A costs and did not recur in 2015; partially offset by:
- decreased expenditures related to forestry control and line clearing on the Company's transmission rights-of-way.

Distribution OM&A Costs

The decrease of $109 million or 14.7% in distribution OM&A costs for the year ended December 31, 2015 was primarily due to the following:

- a decrease in bad debt expense and lower expenditures related to remediation of the Company's customer information system;
- decreased vegetation management expenditures relating to the distribution line clearing and forestry control; and
- lower volume of work associated with locating and restoring power outages; partially offset by
- increased costs associated with responding to power outages as a result of multiple wind storms during the fourth quarter of 2015.

Other OM&A Costs

The increase of $20 million or 35.7% in other OM&A costs for the year ended December 31, 2015 was primarily due to costs to integrate acquired local distribution companies and increased compensation costs.

Depreciation and Amortization

The increase of $37 million or 5.1% in depreciation and amortization costs for the year ended December 31, 2015 compared to last year was mainly due to the growth in capital assets as the Company continues to place new assets in-service, consistent with its ongoing capital investment program.

Income tax expense

Income tax expense for the year ended December 31, 2015 increased by $16 million compared to 2014, and the Company realized an effective tax rate of approximately 12.8% in 2015, compared to approximately 10.6% realized in 2014. The differences are primarily due to the following:

- lower capital cost allowance in excess of depreciation and amortization; and
- additional tax expense in connection with the spin-off of Hydro One Brampton; partially offset by
- an income tax recovery recorded on the revaluation to fair market value of the tax basis of the assets of Hydro One Inc. and its subsidiaries in excess of the Departure Tax triggered when Hydro One exited the PILs Regime.

Hydro One Brampton

On August 31, 2015, a dividend was paid to the Province by transferring to a company wholly-owned by the Province all of the issued and outstanding shares of Hydro One Brampton and inter-company indebtedness owed to Hydro One Inc. by Hydro One Brampton.

Hydro One's 2015 consolidated results of operations include the results of Hydro One Brampton up to August 31, 2015. The following tables present quarterly results of Hydro One Brampton that are included in consolidated results of Hydro One for the years ended December 31, 2015 and 2014.

Quarter ended *(millions of Canadian dollars)*	Mar. 31, 2015	Jun. 30, 2015	Sept. 30, 2015	Dec. 31, 2015	2015 Total
Revenues	125	129	100	–	354
Purchased power	107	111	88	–	306
OM&A	6	6	4	–	16
Depreciation and amortization	5	4	2	–	11
Income tax expense	–	1	(1)	–	–
Net income	7	7	7	–	21
Capital investments	9	11	8	–	28

Quarter ended *(millions of Canadian dollars)*	Mar. 31, 2014	Jun. 30, 2014	Sept. 30, 2014	Dec. 31, 2014	2014 Total
Revenues	127	115	128	125	495
Purchased power	109	99	109	109	426
OM&A	7	6	5	5	23
Depreciation and amortization	4	3	4	3	14
Income tax expense	–	1	–	2	3
Net income	7	6	10	6	29
Capital investments	2	10	6	9	27

Selected Annual Financial Statistics

Year ended December 31 (millions of Canadian dollars, except per share amounts)	2015	2014	2013
Total revenue	6,538	6,548	6,074
Net income attributable to common shareholders	690	731	785
Basic and diluted EPS	$ 1.39	$ 1.53	$ 1.64
Dividends per common share declared	$ 1.83	$ 0.56	$ 0.42
Dividends per preferred share declared	$ 1.03	$ 1.38	$ 1.38
December 31 (millions of Canadian dollars)	2015	2014	2013
Total assets	24,328	22,550	21,625
Total non-current financial liabilities	8,224	8,373	8,301

Quarterly Results Of Operations

The following table sets forth unaudited quarterly information for 2015 and 2014. This information has been derived from the Company's unaudited interim Consolidated Financial Statements and audited annual Consolidated Financial Statements.

Quarter ended *(millions of Canadian dollars)*	Dec. 31, 2015	Sept. 30, 2015	Jun. 30, 2015	Mar. 31, 2015	Dec. 31, 2014	Sept. 30, 2014	Jun. 30, 2014	Mar. 31, 2014
Total revenues	1,522	1,645	1,563	1,808	1,662	1,556	1,566	1,764
Total revenues, net of purchased power	736	789	725	838	769	776	742	842
Net income attributable to common shareholders	143	188	131	228	216	169	110	236
Basic and diluted EPS	$ 0.26	$ 0.39	$0.27	$0.47	$ 0.45	$ 0.35	$ 0.23	$ 0.50

Non-GAAP Measures

FFO and Adjusted FFO

FFO is defined as net cash from operating activities, adjusted for the following: (i) changes in non-cash balances related to operations, (ii) dividends paid on preferred shares, and (iii) distributions to noncontrolling interest. Adjusted FFO is defined as FFO, adjusted for the impact of the deferred income tax asset that resulted as a consequence of leaving the PILs Regime and entering the Federal Tax Regime. Management believes that FFO and adjusted FFO are helpful as supplemental measures of the Company's operating cash flows as they exclude timing-related fluctuations in non-cash operating working capital and cash flows not attributable to common shareholders, and, in the case of adjusted FFO, the impact of the IPO-related deferred income tax asset. As such, these measures provide a consistent measure of the cash generating performance of the Company's assets.

The following table presents the reconciliation of net cash from operating activities to FFO and adjusted FFO:

Year ended December 31 *(millions of Canadian dollars)*	2015	2014
Net cash from (used in) operating activities	(1,253)	1,256
Changes in non-cash balances related to operations	(208)	55
Preferred dividends	(13)	(18)
Distributions to noncontrolling interest	(5)	–
FFO	(1,479)	1,293
Less: Deferred income tax asset[1]	(2,810)	–
Adjusted FFO	1,331	1,293

[1] Impact of deferred income tax asset that resulted as a consequence of leaving the PILs Regime and entering the Federal Tax Regime

Pro forma Adjusted non-GAAP Basic and Diluted EPS

The following pro forma adjusted non-GAAP basic and diluted EPS has been prepared by management on a supplementary basis which assumes that the total number of common shares outstanding was 595,000,000 in each of the years ended December 31, 2015 and 2014. The supplementary pro forma disclosure is used internally by management subsequent to the IPO to assess the Company's performance and is considered useful because it eliminates the impact of the issuance of common shares to the Province prior to the IPO. Prior to the IPO, the Province was the sole shareholder of Hydro One and disclosure of EPS did not provide meaningful information. EPS is considered an important measure and management believes that presenting it for all periods based on the number of outstanding shares on, and subsequent to, the IPO provides users with a basis to evaluate the operations of the Company with comparable companies and with prior periods.

Year ended December 31	2015	2014
Net income attributable to common shareholders *(millions of Canadian dollars)*	690	731
Pro forma weighted average number of common shares		
Basic	595,000,000	595,000,000
Effect of dilutive share grant plans	94,691	–
Diluted	595,094,691	595,000,000
Pro forma adjusted non-GAAP EPS		
Basic	$1.16	$1.23
Diluted	$1.16	$1.23

Adjusted Net Cash from Operating Activities

Adjusted net cash from operating activities is defined as net cash from operating activities, adjusted for the impact of the deferred income tax asset that resulted as a consequence of leaving the PILs Regime and entering the Federal Tax Regime. Management believes that this measure is helpful as a supplemental measure of the Company's net cash from operating activities as it excludes the impact of the IPO-related deferred income tax asset. As such, adjusted net cash from operating activities provides a consistent measure of the Company's cash from operating activities compared to prior periods.

The following table presents the reconciliation of net cash from operating activities to adjusted net cash from operating activities:

Year ended December 31 *(millions of Canadian dollars)*	2015	2014
Net cash from (used in) operating activities	(1,253)	1,256
Less: Deferred income tax asset[1]	(2,810)	–
Adjusted net cash from operating activities	1,557	1,256

[1] Impact of deferred income tax asset that resulted as a consequence of leaving the PILs Regime and entering the Federal Tax Regime

To the extent that adjusted net income is used in future continuous disclosure documents of Hydro One, it will be defined as net income, adjusted for certain items, including non-recurring items and other one-time items that management does not consider to be reflective of the operating performance of the Company. No such adjustments to net income are presented in this MD&A. Management believes that this measure will be helpful in assessing the Company's financial and operating performance in the future.

FFO, adjusted FFO, pro forma adjusted non-GAAP basic and diluted EPS, adjusted net cash from operating activities, and adjusted net income are not recognized measures under US GAAP and do not have a standardized meaning prescribed by US GAAP. They are therefore unlikely to be directly comparable to similar measures presented by other companies. They should not be considered in isolation nor as a substitute for analysis of the Company's financial information reported under US GAAP.

Summary of Sources and Uses of Cash

Hydro One's primary sources of cash flows are funds generated from operations, capital market debt borrowings and bank financing that are used to satisfy Hydro One's capital resource requirements, including the Company's capital expenditures, servicing and repayment of debt, and dividends.

The following table presents the Company's sources and uses of cash during the years ended December 31, 2015 and 2014:

Year ended December 31 *(millions of Canadian dollars)*	2015	2014
Operating activities		
Net income	713	747
Deferred income taxes	(2,844)	10
Changes in non-cash balances related to operations	208	(55)
Other	670	554
	(1,253)	1,256
Financing activities		
Long-term debt issued	350	628
Long-term debt retired	(585)	(776)
Short-term notes issued	1,491	–
Common shares issued	2,600	–
Dividends paid	(888)	(287)
Amount contributed by (distributed to) non-controlling interest	(5)	72
Other	(9)	(32)
	2,954	(395)
Investing activities		
Capital expenditures	(1,632)	(1,504)
Capital contributions	62	–
Acquisitions of local distribution companies	(90)	(66)
Investment in Hydro One Brampton	(53)	–
Proceeds from investment	–	250
Other	6	(6)
	(1,707)	(1,326)
Net change in cash and cash equivalents	(6)	(465)

Cash from Operating Activities

Cash used in operations totalled $1,253 million for 2015 compared to cash from operations of $1,256 million in 2014. Cash from operations was affected by changes in deferred income tax assets that resulted as a consequence of leaving the PILs Regime and entering the Federal Tax Regime. Excluding this effect, cash from operations would have been $1,557 million for 2015, an increase of $301 million compared to prior year, mainly due to improved accounts receivable collections in 2015 and changes in regulatory accounts that impact revenue.

Cash from Financing Activities

Cash from financing activities of $2,954 million for 2015 compared to cash used in financing activities of $395 million in 2014. The increase in 2015 was primarily due to cash proceeds from common shares issued, and the issuance of short-term notes and long-term debt, partly offset by payment of dividends and repayment of long term debt. See section "Liquidity and Financing Strategy" for details of the Company's liquidity and financing strategy.

In 2015, Hydro One issued $350 million of long-term debt under its Medium-Term Note (MTN) Program, compared to $628 million of long-term debt issued in 2014. In 2015, Hydro One repaid $550 million in maturing long-term debt, compared to no long-term debt maturing or repaid in 2014. In addition, long-term debt totalling $35 million assumed as part of the Haldimand County Utilities Inc. (Haldimand Hydro) acquisition and the Woodstock Hydro Holdings Inc. (Woodstock Hydro) acquisition was repaid in 2015.

In 2015, Hydro One paid dividends in the amount of $888 million ($875 million of common share dividends and $13 million of preferred share dividends), compared to dividends totalling $287 million paid in 2014. Included in dividends paid in 2015 was a special dividend paid to the Province prior to the completion of the IPO.

In November 2015, Hydro One issued 2.6 billion common shares to the Province for cash proceeds of $2.6 billion prior to the completion of the IPO.

Cash from Investing Activities

Cash used in investing activities was $1,707 million for 2015 compared to $1,326 million in 2014. The increase in 2015 was mainly due to higher capital investments in 2015 and the sale of an investment in 2014 for $250 million that did not recur in 2015. In 2015, cash totalling $90 million was used to purchase Haldimand Hydro and Woodstock Hydro, compared to cash of $66 million used to purchase Norfolk Power Inc. (Norfolk Power) in 2014. See section "Capital Investments" for details of the Company's capital investments, and section "Other Developments – Acquisitions" for details of the acquisitions of Haldimand Hydro and Woodstock Hydro.

Liquidity and Financing Strategy

Short-term liquidity is provided through funds from operations, Hydro One Inc.'s Commercial Paper Program, and the Company's consolidated credit facilities. Under the commercial paper program, Hydro One Inc. is authorized to issue up to $1.5 billion in short-term notes with a term to maturity of less than 365 days. At December 31, 2015, Hydro One Inc. had $1,491 million in commercial paper borrowings outstanding, compared to no commercial paper borrowings outstanding at December 31, 2014. In addition, the Company and Hydro One Inc. have revolving credit facilities totalling $2,550 million that mature between 2018 and 2020. The Company may use the credit facilities for working capital and general corporate purposes. The short-term liquidity under the Commercial Paper Program, the credit facilities and anticipated levels of funds from operations are expected to be sufficient to fund the Company's normal operating requirements.

At December 31, 2015, all of the Company's long-term debt totalling $8,723 million was issued by Hydro One Inc. under Hydro One Inc.'s MTN Program. At December 31, 2015, the maximum authorized principal amount of medium-term notes issuable under the MTN Program was $3.5 billion, with the entire amount remaining available until January 2018. The long-term debt consists of notes and debentures that mature between 2016 and 2064, and at December 31, 2015, had an average term to maturity of approximately 16.6 years and a weighted average coupon of 4.7%.

At December 31, 2015, Hydro One's corporate credit ratings from approved rating organizations were as follows:

Rating Agency	Corporate Credit Rating
Standard & Poor's Rating Services (S&P)[1]	A

[1] On September 18, 2015, S&P assigned its A corporate credit rating on Hydro One. The outlook is stable.

At December 31, 2015, Hydro One Inc.'s long-term and short-term debt ratings from approved rating organizations were as follows:

Rating Agency	Short-term Debt Rating	Long-term Debt Rating
DBRS Limited (DBRS)[1]	R-1 (low)	A (high)
Moody's Investors Service (Moody's)[2]	Prime-2	A3
S&P[3]	A-1	A

[1] On November 5, 2015, DBRS confirmed Hydro One Inc.'s issuer rating and senior unsecured debenture rating at A (high), downgraded its short-term debt rating to R-1 (low) from R-1 (mid), and revised its trend to stable.

[2] On November 5, 2015, Moody's downgraded the senior unsecured ratings of Hydro One Inc. to A3 from A2, downgraded its short term debt rating to Prime-2 from Prime-1, and revised its outlook on the Company to stable from negative.

[3] On September 18, 2015, S&P affirmed its ratings on Hydro One Inc., including its A long-term corporate credit rating on the company.

At December 31, 2015, Hydro One and Hydro One Inc. were in compliance with all financial covenants and limitations associated with the outstanding borrowings and credit facilities.

Effect of Interest Rates

The Company is exposed to fluctuations in interest rates as its regulated return on equity is derived using a formulaic approach that takes into account anticipated interest rates. See section "Risk Management and Risk Factors – Risks Relating to Hydro One's Business – Market, Financial Instrument and Credit Risk" for more details.

Pension Plan

In 2015, Hydro One contributed approximately $177 million to its pension plan, compared to contributions of approximately $174 million in 2014, and incurred $163 million in net periodic pension benefit costs, compared to $158 million incurred in 2014. The Company estimates that total pension contributions for 2016 will be approximately $180 million.

The Company's pension benefits obligation is impacted by various assumptions and estimates, such as discount rate, rate of return on plan assets, rate of cost of living increase, and mortality assumptions. A full discussion of the significant assumptions and estimates can be found in the section "Critical Accounting Estimates – Employee Future Benefits."

Capital Investments

The Company makes capital investments to maintain the safety, reliability and integrity of its transmission and distribution assets and to provide for the ongoing growth and modernization required to meet the expanding and evolving needs of its customers and the electricity market. This is achieved through a combination of sustaining capital investments, which are required to support the continued operation of Hydro One's existing assets, and development capital investments, which involve both additions to existing assets and large scale projects such as new transmission lines and transmission stations.

In 2015, the Company made capital investments totalling $1,663 million and placed $1,476 million of new assets in-service, including replacements of end-of-life wood poles, new load connections, and the completion of two transformer replacements at the Hanmer Transmission Station, compared to $1,530 million of capital investments and $1,574 million of new assets placed in-service in 2014.

The following table presents Hydro One's 2015 and 2014 capital investments:

Year ended December 31 *(millions of Canadian dollars)*	2015	2014	Change
Transmission			
Sustaining	**706**	625	13.0%
Development	**166**	132	25.8%
Other	**71**	88	(19.3%)
Total Transmission Capital Investments	**943**	845	11.6%
Distribution			
Sustaining	**398**	356	11.8%
Development	**220**	236	(6.8%)
Other	**93**	88	5.7%
Total Distribution Capital Investments	**711**	680	4.6%
Other Capital Investments	**9**	5	80.0%
Total Capital Investments	**1,663**	1,530	8.7%

Transmission Capital Investments

The increase of $98 million or 11.6% in transmission capital investments in 2015 was primarily due to the following:

- several system re-investments, including various end-of-life equipment replacements at certain transmission stations, including the Bruce, Richview, Larchwood and Wiltshire Transmission Stations, as well as the completion of two transformer replacements at the Hanmer Transmission Station;
- the continued work on some of the Company's major inter-area network and local area supply projects, such as the Clarington Transmission Station and Guelph Area Transmission Refurbishment projects;
- increased work on overhead lines refurbishment and replacement projects and programs;
- increased volume of work related to station security upgrades to prevent unauthorized entry to stations and enhance safety, and increased cyber system replacements, including firewall infrastructure, auxiliary equipment and management software, to adhere to the NERC Cyber Security standards; and
- increased volume of demand equipment replacements, as well as spare transformer equipment purchases to ensure readiness for unplanned transformer replacements; partially offset by
- decreased expenditures related to underground lines system replacements, as the end-of-life underground transmission cables between the Strachan Transformer Station and Riverside Junction were replaced and placed in-service in 2014.

Distribution Capital Investments

The increase of $31 million or 4.6% in distribution capital investments in 2015 was primarily due to the following:

- increased capital lines work, primarily related to multiple sustainment initiatives programs and higher volume of component replacements;
- increased work related to station refurbishment programs due to a larger volume of transformer purchases and more refurbishments accomplished during 2015; and
- increased storm restoration work as a result of multiple wind storms which occurred during the fourth quarter of 2015, as well as related power quality-related issues; partially offset by
- decreased expenses in 2015 due to completion of a smart meter installation project in 2014.

Major Transmission Projects

The following table summarizes the status of certain of Hydro One's major transmission projects at December 31, 2015:

Project Name	Location	Type	Anticipated In-Service Date	Estimated Cost	Capital Cost To-Date	Status
Toronto Midtown Transmission Reinforcement	Toronto Southwestern Ontario	New transmission line	2016	$123 million	$121 million	In progress
Guelph Area Transmission Refurbishment	Guelph area Southwestern Ontario	Transmission line upgrade	2016	$103 million	$67 million	In progress
Clarington Transmission Station	Oshawa area Eastern GTA	New transmission station	2018/2019	$297 million	$97 million	In progress
Supply to Essex County Transmission Reinforcement	Windsor Essex area Southwestern Ontario	New transmission line and station	2018	To be determined	–	OEB decision received in July 2015
Northwest Bulk Transmission Line	Thunder Bay Northwestern Ontario	New transmission line	As early as 2020	To be determined	–	Development work is in progress

Future Capital Investments

Hydro One anticipates that it will spend an average of over $1.6 billion per year over the next five years on total capital investments, with sustaining capital investments representing an average of approximately 60% of total capital investments in each year. The Company anticipates that these investments will contribute to improved reliability, customer service and operating efficiencies.

The following table summarizes Hydro One's annual projected capital investments for 2016 to 2020, by business segment:

(millions of Canadian dollars)	2016	2017	2018	2019	2020
Transmission	937	920	978	1,021	989
Distribution	706	692	690	729	663
Other	8	8	7	7	7
Total capital investments	**1,651**	**1,620**	**1,675**	**1,757**	**1,659**

The following table summarizes Hydro One's annual projected capital investments for 2016 to 2020, by category:

(millions of Canadian dollars)	2016	2017	2018	2019	2020
Sustaining	999	998	1,098	1,006	1,001
Development	416	435	360	479	480
Other	236	187	217	272	178
Total capital investments	**1,651**	**1,620**	**1,675**	**1,757**	**1,659**

Note: "Other" capital expenditures consist of special projects, such as those relating to information technology.

Other Obligations

Off-Balance Sheet Arrangements

There are no off-balance sheet arrangements that have, or are reasonably likely to have, a material current or future effect on the Company's financial condition, changes in financial condition, revenues or expenses, results of operations, liquidity, capital expenditures or capital resources.

Summary of Contractual Obligations and Other Commercial Commitments

The following table presents a summary of Hydro One's debt and other major contractual obligations, as well as other major commercial commitments:

December 31, 2015 *(millions of Canadian dollars)*	Total	Less than 1 year	1-3 years	3-5 years	More than 5 years
Contractual obligations *(due by year)*					
Long-term debt – principal repayments	8,723	500	1,350	878	5,995
Long-term debt – interest payments	7,368	397	741	654	5,576
Short-term notes payable	1,491	1,491	–	–	–
Pension contributions[1]	197	180	17	–	–
Environmental and asset retirement obligations[2]	248	22	51	58	117
Outsourcing agreements[3]	523	167	244	101	11
Operating lease commitments	45	11	19	12	3
Other	90	17	34	33	6
Total contractual obligations	18,685	2,785	2,456	1,736	11,708
Other commercial commitments *(by year of expiry)*					
Bank line[4]	2,550	–	800	1,750	–
Letters of credit[5]	154	154	–	–	–
Guarantees[5]	330	330	–	–	–
Total other commercial commitments	3,034	484	800	1,750	–

[1] Contributions to the Hydro One Pension Fund are generally made one month in arrears. The 2016 minimum pension contributions are based on an actuarial valuation as at December 31, 2013 and projected levels of pensionable earnings. Pension contributions beyond 2016 are not estimable at this time.

[2] Hydro One records a liability for the estimated future expenditures associated with the removal and destruction of polychlorinated biphenyl (PCB)-contaminated insulating oils and related electrical equipment, and for the assessment and remediation of chemically-contaminated lands owned by the Company. Hydro One also records a liability for asset retirement obligations associated with the removal and disposal of asbestos-containing materials installed in some of its facilities. The forecasted expenditure pattern reflects the Company's planned work programs for the periods.

[3] Inergi LP (Inergi), an affiliate of Capgemini Canada Inc., provides services to Hydro One, including settlements, source to pay services, pay operations services, information technology, finance and accounting services. The agreement with Inergi for these services expires in December 2019. In addition, Inergi provides customer service operations outsourcing services to Hydro One. The agreement for these services expires in February 2018. Brookfield Global Integrated Solutions (formerly Brookfield Johnson Controls Canada LP) (Brookfield) provides services to Hydro One, including facilities management and execution of certain capital projects as deemed required by the Company. The current agreement with Brookfield expires in December 2024. The contractual amounts disclosed include an estimated contractual annual inflation adjustment in the range of 1.9% to 2.1%. Payments in respect of the Company's outsourcing agreements are recorded in OM&A costs on the Company's Consolidated Statements of Operations and Comprehensive Income or as a cost of capital programs.

[4] The Company and Hydro One Inc. have revolving credit facilities totalling $2,550 million that expire between 2018 and 2020.

[5] Hydro One Inc. currently has outstanding bank letters of credit of $139 million relating to retirement compensation arrangements. Hydro One Inc. provides prudential support to the IESO in the form of letters of credit, the amount of which is calculated based on forecasted monthly power consumption. At December 31, 2015, Hydro One Inc. has provided a letter of credit to the IESO in the amount of $15 million to meet its current prudential requirements. Hydro One Inc. has also provided prudential support to the IESO on behalf of its subsidiaries as required by the IESO's Market Rules, using parental guarantees of $329 million, and on behalf of a distributor using total guarantees of $1 million.

Regulation

The OEB approves both the revenue requirements of and the rates charged by Hydro One's regulated transmission and distribution businesses. The rates are designed to permit the Company's transmission and distribution businesses to recover the allowed costs and to earn a formula-based annual rate of return on its equity invested in the regulated businesses. This is done by applying a specified equity risk premium to forecasted interest rates on long-term bonds. In addition, the OEB approves rate riders to allow for the recovery or disposition of specific regulatory deferral accounts over specified timeframes.

The following table summarizes Hydro One's major regulatory proceedings:

Application	Year(s)	Type	Status
Electricity Rates			
Hydro One Networks	2015-2016	Transmission – Cost-of-service	OEB decision received
Hydro One Networks	2015-2017	Distribution – Custom	OEB decision received
B2M LP	2015	Transmission – Interim	OEB decision received
B2M LP	2015-2019	Transmission – Cost-of-service	OEB decision received
Mergers Acquisitions Amalgamations and Divestitures			
Haldimand Hydro	n/a	Acquisition	OEB decision received
Woodstock Hydro	n/a	Acquisition	OEB decision received
Leave to Construct			
Supply to Essex County Transmission Reinforcement Project	n/a	Section 92	OEB decision received

Hydro One has secured rate orders for Hydro One Networks' transmission business through 2016, for B2M LP through 2019, and for Hydro One Networks' distribution business to the end of 2017.

The following table summarizes the status of Hydro One's electricity rate applications.

Application	Date of Rate Application Approval	Year	ROE Allowed (A) or Forecast (F)	Rate Base	Date of Rate Order Filing	Rate Order Status
Transmission:						
Hydro One Networks	January 2015	2015	9.30% (A)	$9,651 million	January 2015	Approved
		2016	9.19% (A)	$10,040 million	November 2015	Approved
B2M LP	December 2015	2015	9.30% (A)	$523 million	December 2014	Approved
		2016	9.19% (A)	$516 million	January 2016	Approved
		2017	9.71% (F)	$509 million	–	To be filed 2016 Q4
		2018	9.96% (F)	$502 million	–	To be filed 2017 Q4
		2019	10.01% (F)	$496 million	–	To be filed 2018 Q4
Distribution:						
Hydro One Networks	March 2015	2015	9.30% (A)	$6,552 million	April 2015	Approved
		2016	9.19% (A)	$6,863 million	January 2016	Approved
		2017	9.71% (F)	$7,190 million	–	To be filed 2016 Q4

Hydro One Networks

Hydro One Networks' transmission 2016 revenue requirement of $1,480 million is reflected in the Uniform Transmission Rates (UTR) Decision and Order. Hydro One Networks plans to submit a transmission application for 2017-2018 rates in the second quarter of 2016.

The Hydro One Distribution forecast for 2017 will be subject to adjustments for cost of capital parameters. Hydro One Networks plans to submit a distribution application for 2018-2022 rates in the first quarter of 2017.

B2M LP

On December 29, 2015, the OEB issued a Decision and Order approving the five-year revenue requirement for years 2015-2019 inclusive, approving the recovery of $8 million start-up costs in rates, and the establishment of a deferral account to capture costs of Tax Rate and Rule changes. The January 14, 2016, Decision and Rate Order approved the B2M LP revenue requirement recovery through the 2016 UTRs.

Supply to Essex County Transmission Reinforcement Project

On July 16, 2015, the OEB issued a Decision and Order granting Hydro One Networks leave to Construct a new 13-kilometre 230 kV double-circuit transmission line in the Windsor-Essex region. The Decision and Order includes standard conditions of adherence to the system impact assessment and the connection impact assessment, and requires construction to commence within twelve months. In addition, on August 28, 2015, the OEB issued a letter stating that given the complexities and implications of the issues relating to cost allocation, including potential changes to the provisions in the Distribution System Code and the Transmission System Code, the OEB will not proceed with cost allocation through an adjudicative process, but will review these issues from a policy perspective.

On January 7, 2016, the OEB initiated its policy review. In the southeast Essex County, a number of large distribution-connected customers are a factor driving the need for new transmission capacity, such as the new Leamington transmission station. Three other distributors embedded in Hydro One's distribution area will also benefit from this investment. Therefore, Hydro One has proposed that its share of this transmission investment be shared proportionately between Hydro One and the other identified beneficiaries in the area. The OEB consultation will review the concept of proportional benefit and its application, as the policy and regulatory framework to flow transmission costs through to identified distribution-connected customers is not in place.

Other Regulatory Developments

Time-of-Use (TOU) Pricing Decision and Order

On March 26, 2015, the OEB issued a Decision and Order to amend Hydro One Networks' distribution license to include an exemption from the requirement to apply TOU pricing to approximately 170,000 Regulated Price Plan customers that are outside the smart meter telecommunications infrastructure. The exemption expires December 31, 2019.

Distribution System Code Requirements

In April 2015, the OEB introduced a Notice of Amendment to the Distribution System Code requiring electricity distributors to issue monthly bills to non-seasonal residential and certain general service customers by the end of 2016. In addition, the OEB amended the Distribution System Code imposing a 98% billing accuracy requirement, and provisions allowing a local distribution company to issue a bill based on estimated consumption only twice every twelve months to these customers. In September 2015, the OEB issued its Decision and Order amending Hydro One Networks' electricity distribution licence to include an exemption from the requirement for estimated billing and billing accuracy for the 170,000 hard-to-reach customers that are currently exempt from TOU billing, for a term ending on December 31, 2019.

On December 31, 2015, Hydro One submitted a report to the OEB summarizing that as of November 2015, approximately only 101,000 "hard-to-reach" customers received estimated bills in 2015 and significant improvements were realized in estimated billing accuracy due to the availability of better customer-specific historical usage data on which the estimation algorithms are based.

Conservation and Demand Management

In accordance with a directive from the Minister of Energy and Infrastructure dated March 31, 2010, as a condition of licence, certain licensed electricity distributors must meet the IESO established targets for the reduction of electricity consumption and peak provincial electricity demand. On September 30, 2015, Hydro One Networks filed its annual Conservation and Demand Management (CDM) Report with the OEB. In 2014, Hydro One Networks achieved 167.4 MW in peak demand savings and 898.4 GWh in energy savings, which represent 78.4% and 79.5% of its peak demand and energy reduction targets, respectively. Although Hydro One Networks did not meet its peak demand reduction target, no punitive action will be taken against the Company.

Rate Design (previously Revenue Decoupling for Distributors)

In April 2015, the OEB issued a report, *"Board Policy: A New Distribution Rate Design for Residential Electricity Customers"*, outlining its new policy on fully fixed distribution charges for residential customers. The current distribution charges are a combination of fixed and variable rates. Under the new policy, electricity distributors will structure their residential rates such that all distribution service costs will be collected through a fixed monthly charge only. The new policy will be implemented gradually over a four year period, with increases in the fixed rate and decreases in the variable rate, resulting in a fixed rate only by 2019. The new rate design will enable residential customers to leverage new technologies, manage costs through conservation, and better understand the value of distribution services. It will also provide greater revenue stability for distributors, including Hydro One.

In its December 22, 2015 Decision, the OEB has increased the transition period for Hydro One Networks' certain customer classes to eight years to mitigate excessive bill impacts.

In January 2016, the OEB issued a Decision and Rate Order for the area formerly served by Norfolk Power approving Hydro One's implementation plan to transition residential customers to fixed rates over a four year period. Although Norfolk Power customers' rates are frozen for five years, the OEB Order approved Tariffs of Rates and Charges for 2016 only.

In 2015, Hydro One Networks filed applications with the OEB with respect to the new rate design for residential customers in the service areas formerly served by Haldimand Hydro and Woodstock Hydro that include fixed rates for five years and implementation plans to transition to fixed distribution rates. Approvals for these applications are pending.

Performance Measurement for Electricity Distributors

On September 18, 2015, Hydro One Networks submitted its 2014 Performance Scorecard to the OEB. In addition to ongoing operations, a major focus in 2014 was investing in improvements to the Company's customer call centre and billing operations. Hydro One plans to continue developing targeted products and services that respond to its customers' unique needs, including realizing value from the new customer information system, simplifying and shortening timeframes for the delivery of services, and enhancing accessibility to allow effective self-service for simple transactions. The Company is also committed to delivering programs to help its customers manage their energy consumption. Hydro One Networks' 2014 Scorecard was posted on the Hydro One and the OEB websites.

Renewed Regulatory Framework for Transmitters

In 2015, the OEB initiated a discussion to develop a framework for the application of Renewed Regulatory Framework principles to transmitters, and in January 2016, issued a new set of draft filing requirements for transmitters for discussion.

Transmitter Consolidations

On January 19, 2016, the OEB issued the *Handbook for Electricity Distributor and Transmitter Consolidations* (the "handbook") to provide guidance on applications for approval of electricity utility consolidations by way of mergers, acquisitions, amalgamations and divestitures and subsequent rate applications. The handbook is intended to provide guidance on the process for review of consolidation applications by the OEB and affirms the OEB's policy of using the "no harm" test in reviewing consolidation applications. This test requires applicants to demonstrate that the costs to serve acquired customers post-consolidation will be no higher than they otherwise would be without consolidation. In addition the OEB will consider whether any price premium paid on the acquisition is financially burdensome to the applicant, as any premium paid over historic asset value is not recoverable in rates. The handbook will allow applicants to defer rebasing of the acquired utility for up to a 10 year period with the view of permitting the applicant to fully realize the anticipated efficiency gains and offset the overall costs of the transaction.

Other Developments

Change in Hydro One Ownership Structure

During the fourth quarter of 2015, Hydro One and Hydro One Inc. completed a series of Pre-Closing Transactions that resulted in, among other things, the acquisition by Hydro One of all of the issued and outstanding shares of Hydro One Inc. and the issuance of new common shares and preferred shares of Hydro One to the Province. On November 5, 2015, Hydro One and the Province concluded the IPO of Hydro One on the Toronto Stock Exchange, whereby 81.1 million of the 595 million outstanding common shares of Hydro One were sold to the public. On November 12, 2015, the underwriters of the IPO exercised their option to purchase an additional 8.15 million common shares of Hydro One from the Province. All proceeds from the IPO were received by the Province. All of the regulated business and outstanding notes and debentures of Hydro One at the time of the IPO remain at Hydro One Inc. The final prospectus associated with the IPO, which contains details of the IPO, recapitalization and corporate structure, is posted on www.sedar.com.

PILs Deemed Disposition Rules

In connection with the IPO, upon ceasing to be exempt from tax under the Federal Tax Regime in October 2015, Hydro One and its subsidiaries were deemed to dispose of their assets for proceeds equal to their fair market value, triggering a PILs liability of $2.6 billion (Departure Tax). The Departure Tax amount was confirmed in writing by the Minister of Finance and was paid to the OEFC in 2015. To enable Hydro One and its subsidiaries to pay the Departure Tax, the Province made an equity injection of $2.6 billion in Hydro One and received 2.6 billion common shares of Hydro One. The revaluation of the tax basis of the assets of Hydro One Inc. and its subsidiaries to fair market value resulted in a net deferred tax recovery of $2,619 million recorded in 2015.

Class Action Lawsuit

In September 2015, Hydro One and three of its subsidiaries were served with a class action suit in which the representative plaintiff is seeking up to $125 million in damages related to allegations of improper billing practices. Hydro One intends to defend the action. Due to the preliminary stage of legal proceedings, an estimate of a possible loss related to this claim cannot be made.

Acquisitions

Integration of Norfolk Power

The Company acquired Norfolk Power in August 2014. The purchase price for Norfolk Power, adjusted for working capital and other closing adjustments, was approximately $68 million. Due to this acquisition, approximately 18,000 new customers were added to Hydro One's Distribution Business. In September 2015, the Company completed the integration of Norfolk Power, including the integration of employees, customers, business processes, information and operations. This successful integration will allow the Company to standardize processes and leverage key lessons learned to drive efficiency and improvements when integrating other acquisitions in the future.

Acquisition of Haldimand Hydro

In June 2015, Hydro One completed the acquisition of Haldimand Hydro, an electricity distribution company located in southwestern Ontario, following approval of the acquisition by the OEB in March 2015. The purchase price for Haldimand Hydro, adjusted for working capital and other closing adjustments of approximately $8 million, was approximately $73 million. The goodwill of approximately $33 million arising from the Haldimand Hydro acquisition consists largely of the synergies and economies of scale expected from combining the operations of Hydro One and Haldimand Hydro. Due to this acquisition, approximately 21,000 new customers were added to Hydro One's Distribution Business. Integration of Haldimand Hydro is ongoing.

Acquisition of Woodstock Hydro

In October 2015, Hydro One completed the acquisition of Woodstock Hydro, an electricity distribution company located in southwestern Ontario, following approval of the acquisition by the OEB in September 2015. The purchase price for Woodstock Hydro, adjusted for preliminary working capital and other closing adjustments, was approximately $32 million. The preliminary goodwill of approximately $17 million arising from the Woodstock Hydro acquisition consists largely of the synergies and economies of scale expected from combining the operations of Hydro One and Woodstock Hydro. Due to this acquisition, approximately 16,000 new customers were added to Hydro One's Distribution Business. Integration of Woodstock Hydro is ongoing.

Great Lakes Power Transmission Purchase Agreement

On January 28, 2016, Hydro One reached an agreement to acquire from Brookfield Infrastructure various entities that own and control Great Lakes Power Transmission LP, an Ontario regulated electricity transmission business operating along the eastern shore of Lake Superior, north and east of Sault Ste. Marie, Ontario, for $222 million in cash, subject to customary adjustments, plus the assumption of approximately $151 million in outstanding indebtedness. The acquisition is pending a *Competition Act* approval as well as regulatory approval from the OEB.

Hydro One Workforce

Hydro One has a skilled and flexible work force of over 5,500 regular employees and over 2,000 non-regular employees province-wide, comprising a mix of skilled trades, lines staff, engineering, professional, managerial and executive personnel. Hydro One's regular employees are supplemented primarily by accessing a large external labour force available through arrangements with the Company's trade unions for variable workers, sometimes referred to as "hiring halls", and also by access to contract personnel. The hiring halls offer Hydro One the ability to access highly trained and appropriately skilled workers on a project-by-project and seasonal basis.

The following table sets out the number of Hydro One employees as at December 31, 2015.

	Regular Employees	Non-Regular Employees	Total
Power Workers' Union (PWU)	3,419	636[1]	4,055
The Society of Energy Professionals (Society)	1,394	57	1,451
Canadian Union of Skilled Workers (CUSW) and construction building trade unions[2]	–	1,346	1,346
International Brotherhood of Electrical Workers (IBEW)	63	4	67
Total employees represented by unions	4,876	2,043	6,919
Management and non-represented employees	640	34	674
Total employees	5,516	2,077	7,593

[1] Includes 475 non-regular "hiring hall" employees covered by PWU agreement.

[2] Employees are jointly represented by both unions. The construction building trade unions have collective agreements with the Electrical Power Systems Construction Association (EPSCA).

Collective Agreements

The PWU represents the majority of the skilled trade personnel employed by Hydro One. In April 2015, Hydro One reached an agreement with the PWU for a renewal of the collective agreement. The agreement is for a three-year term, covering April 1, 2015 to March 31, 2018. The agreement was ratified by the PWU and the Hydro One Board of Directors in July 2015.

The Society represents professional and certain first-level supervisory staff employed by Hydro One. In July 2015, Hydro One reached an agreement with the Society for an early renewal of the collective agreement. The agreement is for a three-year term, covering April 1, 2016 to March 31, 2019. The agreement was ratified by the Society and the Hydro One Board of Directors in August 2015.

In July 2015, Hydro One reached an agreement with the CUSW for a renewal of the collective agreement. The agreement is for a three-year term, covering May 1, 2014 to April 30, 2017. The agreement was ratified by CUSW in September 2015 and the Hydro One Board of Directors in August 2015.

The EPSCA is an employers' association of which Hydro One is a member. A number of the EPSCA construction collective agreements, which bind Hydro One, expired in April 2015. Ratified five-year renewal collective agreements, covering May 1, 2015 to April 30, 2020, have been reached with The United Association of Plumbers and Pipefitters, The Ironworkers, The Rodmen, The Boilermakers, The Insulators, The Sheet Metal Workers, The Roofers, the Labourers International Union of North America (LIUNA), the Operating Engineers (OE) and the Teamsters.

Share-based Compensation

Share Grant Plans

At December 31, 2015, Hydro One had two share grant plans, one for the benefit of certain members of the Power Workers' Union (the PWU Share Grant Plan) and one for the benefit of certain members of The Society of Energy Professionals (the Society Share Grant Plan).

The PWU Share Grant Plan provides for the issuance of common shares of Hydro One from treasury to certain eligible members of the PWU annually, commencing on April 1, 2017 and continuing until the earlier of April 1, 2028 or the date an eligible employee no longer meets the eligibility criteria of the PWU Share Grant Plan. The number of common shares granted annually to each eligible employee will be equal to 2.7% of such eligible employee's salary as at April 1, 2015, divided by the price of the common shares of Hydro One in the IPO. The aggregate number of common shares issuable under the PWU Share Grant Plan shall not exceed 3,981,763 common shares.

The Society Share Grant Plan provides for the issuance of common shares of Hydro One from treasury to certain eligible members of the Society annually, commencing on April 1, 2018 and continuing until the earlier of April 1, 2029 or the date an eligible employee no longer meets the eligibility criteria of the Society Share Grant Plan. The number of common shares granted annually to each eligible employee will be equal to 2.0% of such eligible employee's salary as at September 1, 2015, divided by the price of the common shares of Hydro One in the IPO. The aggregate number of common shares issuable under the Society Share Grant Plan shall not exceed 1,434,686 common shares.

Directors' Deferred Share Unit (DSU) Plan

Under the Company's Directors' DSU Plan, directors can elect to receive credit for their annual cash retainer in a notional account of DSUs in lieu of cash. Hydro One's Board of Directors may also determine from time to time that special circumstances exist that would reasonably justify the grant of DSUs to a director as compensation in addition to any regular retainer or fee to which the director is entitled.

Employee Share Ownership Plan

Effective December 15, 2015, Hydro One established an Employee Share Ownership Plan (ESOP). Under the ESOP, certain eligible management and non-represented employees may contribute between 1% and 6% of their base salary towards purchasing common shares of Hydro One. The Company will match 50% of the employee's contributions, up to maximum Company contribution of $25,000 per calendar year. No contributions were made under the ESOP during 2015.

Long-term Incentive Plan

The Board of Directors of Hydro One adopted a Long-term Incentive Plan effective August 31, 2015. Under the Long-term Incentive Plan, long-term incentives will be granted to certain executive and management employees, and all equity-based awards will be settled in newly-issued shares of Hydro One from treasury, consistent with the provisions of the plan.

The mix of long-term incentive vehicles has not yet been determined and, accordingly, the Long-term Incentive Plan provides flexibility to award a range of vehicles, including restricted share units, performance share units, stock options, share appreciation rights, restricted shares, deferred share units and other share-based awards. The mix of vehicles is intended to vary by role to recognize the level of executive accountability for overall business performance. It is expected that the specific incentive vehicles and performance targets associated with the Long-term Incentive Plan will be decided in early 2016, after which the incentive grants will commence. No long-term incentive payments were awarded during 2015.

Related Party Transactions

The Province is the majority shareholder of Hydro One. The OEFC, IESO, Ontario Power Generation Inc. (OPG), the OEB, and Hydro One Brampton are related parties to Hydro One because they are controlled or significantly influenced by the Province. The following is a summary of the Company's related party transactions during the year ended December 31, 2015:

The Province

- During 2015, Hydro One paid dividends to the Province totalling $888 million (2014 – $287 million). In addition, on August 31, 2015, Hydro One declared a dividend in-kind on its common shares payable in all of the issued and outstanding shares of Hydro One Brampton.
- On November 4, 2015, Hydro One issued 2.6 billion common shares to the Province for proceeds of $2.6 billion.
- In 2015, Hydro One Inc. incurred certain IPO related expenses totaling $7 million which will be reimbursed to the Company by the Province and reimbursed by the Company to Hydro One Inc.

IESO

- During 2015, Hydro One purchased power in the amount of $2,318 million from the IESO-administered electricity market, compared to $2,601 million purchased in 2014.
- Hydro One receives revenues for transmission services from the IESO, based on OEB-approved Uniform Transmission Rates. The Company's 2015 transmission revenues include $1,548 million related to these services, compared to $1,556 million in 2014.
- Hydro One receives amounts for rural rate protection from the IESO. The Company's 2015 distribution revenues include $127 million related to this program, compared to $127 million in 2014.
- Hydro One receives revenues related to the supply of electricity to remote northern communities from the IESO. The Company's 2015 distribution revenues include $32 million related to these services, compared to $32 million in 2014.
- The IESO (Ontario Power Authority prior to January 1, 2015) funds substantially all of Hydro One's CDM programs. The funding includes program costs, incentives, and management fees. During 2015, the Company received $70 million related to these programs, compared to $33 million received in 2014.

OPG

- During 2015, Hydro One purchased power in the amount of $11 million from the OPG, compared to $23 million purchased in 2014.
- Hydro One has service level agreements with OPG. These services include field, engineering, logistics and telecommunications services. The Company's other 2015 revenues include $7 million related to these service level agreements, compared to $12 million in 2014. OM&A costs related to the purchase of services with respect to these service level contracts were not significant in 2015 and 2014.

OEFC

- During 2015, Hydro One made PILs to the OEFC totalling $2.9 billion, including Departure Tax of $2.6 billion, compared to payments of $86 million made in 2014.
- During 2015, Hydro One purchased power in the amount of $6 million from power contracts administered by the OEFC, compared to $9 million purchased in 2014.
- In 2015, the Company paid $8 million to the OEFC, compared to $5 million paid in 2014, for indemnification against adverse claims in excess of $10 million paid by the OEFC with respect to certain of Ontario Hydro's businesses transferred to Hydro One on April 1, 1999. Hydro One has not made any claims under the indemnity since it was put in place in 1999. Hydro One and the OEFC, with the consent of the Minister of Finance, have agreed to terminate the indemnity effective October 31, 2015.

OEB

- Under the *OEB Act*, the OEB is required to recover all of its annual operating costs from gas and electricity distributors and transmitters. During 2015, Hydro One incurred $12 million in OEB fees, compared to $12 million incurred in 2014.

Hydro One Brampton

- Effective August 31, 2015, Hydro One Brampton is no longer a subsidiary of Hydro One Inc., but is indirectly owned by the Province. Subsequent to August 31, 2015, Hydro One continues to provide certain management, administrative and smart meter network services to Hydro One Brampton pursuant to certain service level agreements, which are provided at market rates. During 2015, revenues related to the provision of services with respect to these service level agreements were $1 million.

At December 31, 2015, the amounts due from and due to related parties as a result of the transactions described above were $191 million and $138 million, compared to $224 million and $227 million at December 31, 2014, respectively. At December 31, 2015, included in amounts due to related parties were amounts owing to the IESO in respect of power purchases of $134 million, compared to $214 million at December 31, 2014.

Risk Management and Risk Factors

Risks Relating to Hydro One's Business

Regulatory Risks and Risks Relating to Hydro One's Revenues

Risks Relating to Obtaining Rate Orders

The Company is subject to the risk that the OEB will not approve the Company's transmission and distribution revenue requirements requested in future applications for rates. Rate applications for revenue requirements are subject to the OEB's review process, usually involving participation from intervenors and a public hearing process. There can be no assurance that resulting decisions or rate orders issued by the OEB will permit Hydro One to recover all costs actually incurred, including operations, maintenance and administration costs, costs accumulated in other regulatory accounts (including, for instance, deferral and variance accounts), costs of debt and income taxes, or to earn a particular return on equity. A failure to obtain acceptable rate orders, or approvals of appropriate returns on equity and costs actually incurred, may materially adversely affect: Hydro One's transmission or distribution businesses, the undertaking or timing of capital expenditures, ratings assigned by credit rating agencies, the cost and issuance of long-term debt, and other matters, any of which may in turn have a material adverse effect on the Company. In addition, there is no assurance that the Company will receive regulatory decisions in a timely manner and, therefore, costs may be incurred prior to having an approved revenue requirement.

Risks Relating to Actual Performance Against Forecasts

The Company's ability to recover the actual costs of providing service and earn the allowed return on equity depends on the Company achieving its forecasts established and approved in the rate-setting process. Actual costs could exceed the approved forecasts if, for example, the Company incurs operations, maintenance and administration costs above those included in the Company's approved revenue requirement, higher capital expenditures than those approved in rate decisions, or additional financing charges because of increased debt amounts or higher interest rates. The inability to obtain acceptable rate decisions or to otherwise recover any significant difference between forecast and actual expenses could materially adversely affect the Company's financial condition and results of operations.

Further, the OEB approves the Company's transmission and distribution rates based on projected electricity load and consumption levels, among other factors. If actual load or consumption materially falls below projected levels, the Company's revenue and net income for either, or

both, of these businesses could be materially adversely affected. Also, the Company's current revenue requirements for these businesses are based on cost and other assumptions that may not materialize. There is no assurance that the OEB would allow rate increases sufficient to offset unfavourable financial impacts from unanticipated changes in electricity demand or in the Company's costs.

The Company is subject to risk of revenue loss from other factors, such as economic trends and weather conditions that influence the demand for electricity. The Company's overall operating results may fluctuate substantially on a seasonal and year-to-year basis based on these trends and weather conditions. For instance, a cooler than normal summer or warmer than normal winter may reduce demand for electricity below that forecast by the Company, causing a decrease in the Company's revenues from the same period of the previous year. The Company's load could also be negatively affected by successful CDM programs whose results exceed forecasted expectations.

Risks Relating to Rate-Setting Models for Transmission and Distribution

The OEB's rate-setting model for distributors requires that the term of a custom rate application (distribution business) be a minimum five-year period. There are risks associated with forecasting over such a long period. For instance, if unanticipated capital expenditures arise that were not contemplated in the Company's most recent rate decision, the Company may be required to incur costs that may not be recoverable until a future period or not recoverable at all in future rates. This could have a material adverse effect on the Company.

The OEB has stated its intention to examine the policies that may apply to transmission rate setting, and this may result in changes to the rate-setting model for transmission services. A change to the rate-setting model for transmission services, such as the introduction of an asymmetrical earnings sharing mechanism, could result in a decrease in the Company's revenues or financial performance.

The OEB approves and periodically, generally on an annual basis, changes the return on equity for transmission and distribution businesses. The OEB may in the future decide to reduce its allowed return on equity for either of these businesses, modify the formula or methodology it uses to determine the return on equity, or reduce the weighting of the equity component of the deemed capital structure. Any such reduction could reduce the net income of the Company.

Risks Relating to Capital Expenditures

In order to be recoverable, capital expenditures require the approval of the OEB, either through the approval of capital expenditure plans, rate base or revenue requirements for the purposes of setting transmission and distribution rates, which include the impact of capital expenditures on rate base or cost of service. There can be no assurance that all capital expenditures incurred by Hydro One will be approved by the OEB. Capital cost overruns may not be recoverable in transmission or distribution rates. The Company could incur unexpected capital expenditures in maintaining or improving its assets, particularly given that new technology is required to support renewable generation and unforeseen technical issues may be identified through implementation of projects. There is risk that the OEB may not allow full recovery of such expenditures in the future. To the extent possible, Hydro One aims to mitigate this risk by ensuring prudent expenditures, seeking from the regulator clear policy direction on cost responsibility, and pre-approval of the need for capital expenditures.

While the Company expects all of its expenditures and regulatory assets to be fully recoverable after OEB review, any future regulatory decision to disallow or limit the recovery of such costs would lead to a lower than expected approved revenue requirement or rate base, potential asset impairment or charges to the Company's results of operations, any of which could have a material adverse effect on the Company.

Risks Relating to Deferred Tax Asset

As a result of leaving the PILs Regime and entering the Federal Tax Regime, Hydro One recorded a deferred tax asset due to the revaluation of the tax basis of Hydro One's fixed assets at their fair market value and recognition of eligible capital expenditures. Management believes this will result in annual net cash savings over the next five years due to the reduction of cash taxes payable by Hydro One associated primarily with a higher capital cost allowance. There is a risk that, in future rate applications, the OEB will reduce the Company's revenue requirement by all or a portion of those net cash savings. If the OEB were to reduce the Company's revenue requirement in this manner, it could have a material adverse effect on the Company.

Risks Relating to Other Applications to the OEB

The Company is also subject to the risk that it will not obtain required regulatory approvals for other matters, such as leave to construct applications, applications for mergers, acquisitions, amalgamations and divestitures, and environmental approvals. Decisions to acquire or divest other regulated businesses licensed by the OEB are subject to OEB approval. Accordingly, there is the risk that such matters may not be approved or that unfavourable conditions will be imposed by the OEB.

First Nations and Métis Claims Risk

Some of the Company's current and proposed transmission and distribution assets are or may be located on Reserve (as defined in the *Indian Act* (Canada)) lands, and lands over which First Nations and Métis have Aboriginal, treaty or other legal claims. Although the Company has a recent history of successful negotiations and engagement with First Nations and Métis communities in Ontario, some First Nations and Métis leaders, communities and their members have made assertions related to sovereignty and jurisdiction over Reserve lands and traditional territories and are increasingly willing to assert their claims through the courts, tribunals, or by direct action. These claims could have a material adverse effect on the Company or otherwise materially adversely impact the Company's operations, including the development of current and future projects.

The Company's operations and activities may, on occasion, give rise to the Crown's duty to consult and potentially accommodate First Nations and Métis communities. Procedural aspects of the duty to consult may be delegated to the Company by the Province or the federal government. A perceived failure by the Crown to sufficiently consult a First Nations or Métis community, or a perceived failure by the Company in relation to delegated consultation obligations, could result in legal challenges against the Crown or the Company, including judicial review or injunction proceedings, or could potentially result in direct action against the Company by a community or its members. If this occurs, it could disrupt or delay the Company's operations and activities, including current and future projects, and have a material adverse effect on the Company.

Risk from Transfer of Assets Located on Reserves

The transfer orders by which the Company acquired certain of Ontario Hydro's businesses as of April 1, 1999 did not transfer title to assets located on Reserves. The transfer of title to these assets did not occur because authorizations originally granted by the federal government for the construction and operation of these assets on Reserves could not be transferred without required consent. In several cases, the authorizations had either expired or had never been issued.

Currently, the Ontario Electricity Financial Corporation holds legal title to these assets and it is expected that the Company will manage them until it has obtained permits to complete the title transfer. To occupy Reserves, the Company must have valid permits issued by Her Majesty the Queen in the Right of Canada. For each permit, the Company must negotiate an agreement (in the form of a memorandum of understanding) with the First Nation, the Ontario Electricity Financial Corporation and any members of the First Nation who have occupancy rights. The agreement includes provisions whereby the First Nation consents to the federal government (presently Indigenous Affairs and Northern Development Canada) issuing a permit. For transmission assets, the Company must negotiate terms of payment. It is difficult to predict the aggregate amount that the Company may have to pay, either on an annual or one-time basis, to obtain the required agreements from First Nations. If the Company cannot reach satisfactory agreements with the relevant First Nation to obtain federal permits, it may have to relocate these assets to other locations at a cost that could be substantial. In a limited number of cases, it may be necessary to abandon a line and replace it with diesel generation facilities. In either case, the costs relating to these assets could have a material adverse effect on the Company if the costs are not recoverable in future rate orders.

Compliance with Laws and Regulations

Hydro One must comply with numerous laws and regulations affecting its business, including requirements relating to transmission and distribution companies, environmental laws, employment laws and health and safety laws. The failure of the Company to comply with these laws could have a material adverse effect on the Company's business. See also "– Health, Safety and Environmental Risk".

For instance, Hydro One's licensed transmission and distribution businesses are required to comply with the terms of their licenses, with codes and rules issued by the OEB, and with other regulatory requirements, including regulations of the National Energy Board. In Ontario, the Market Rules issued by the IESO require the Company to, among other things, comply with the reliability standards established by the NERC and Northeast Power Coordinating Council, Inc. (NPCC). The incremental costs associated with compliance with these reliability standards are expected to be recovered through rates, but there can be no assurance that the OEB will approve the recovery of all of such incremental costs. Failure to obtain such approvals could have a material adverse effect on the Company.

There is the risk that new legislation, regulations or policies will be introduced in the future. These may require Hydro One to incur additional costs, which may or may not be recovered in future transmission and distribution rates.

Risk of Natural and Other Unexpected Occurrences

The Company's facilities are exposed to the effects of severe weather conditions, natural disasters, man-made events including but not limited to cyber and physical terrorist type attacks, events which originate from third party connected systems, or any other potentially catastrophic events. Although constructed, operated and maintained to industry standards, the Company's facilities may not withstand

occurrences of this type in all circumstances. The Company does not have insurance for damage to its transmission and distribution wires, poles and towers located outside its transmission and distribution stations resulting from these or other events. Losses from lost revenues and repair costs could be substantial, especially for many of the Company's facilities that are located in remote areas. The Company could also be subject to claims for damages caused by its failure to transmit or distribute electricity. Hydro One's risk is partly mitigated because its transmission system is designed and operated to withstand the loss of any major element and possesses inherent redundancy that provides alternate means to deliver large amounts of power. In the event of a large uninsured loss, Hydro One would apply to the OEB for recovery of such loss; however, there can be no assurance that the OEB would approve any such applications, in whole or in part, which could have a material adverse effect on the Company.

Risk Associated with Information Technology Infrastructure and Data Security

The Company's ability to operate effectively in the Ontario electricity market is, in part, dependent upon it developing, maintaining and managing complex information technology systems which are employed to operate and monitor its transmission and distribution facilities, financial and billing systems and other business systems. The Company's increasing reliance on information systems and expanding data networks increases its exposure to information security threats. The Company's transmission business is required to comply with various rules and standards for transmission reliability, including mandatory standards established by the NERC and the NPCC. These include standards relating to cyber security and information technology, which only apply to certain of the Company's assets (generally being those whose failure could impact the functioning of the bulk electricity system). The Company may maintain different or lower levels of information technology security for its assets that are not subject to these mandatory standards. Unauthorized access to corporate and information technology systems or cyber-attacks could result in service disruptions and system failures, which could have a material adverse effect on the Company, including as a result of a failure to provide electricity to customers. In addition, in the normal course of its operations, the Company may collect, process or retain access to confidential customer, supplier, counterparty or employee information, which could be exposed in the event of a cyber security incident.

Hydro One mitigates these risks, including through the use of security event management tools on its power and business systems, by separating its transmission and distribution system networks from its other business system networks, by performing scans of its systems for known cyber threats and by providing company-wide awareness training to Hydro One personnel. Hydro One also engages the services of external experts to evaluate the security of its information technology infrastructure and controls. Hydro One performs vulnerability assessments on its critical cyber assets and it ensures security and privacy controls are incorporated into new information technology capabilities. Although these security and system disaster recovery controls are in place, there can be no assurance that there will not be system failures or security breaches or that such threats would be detected or mitigated on a timely basis. Upon occurrence and detection, the focus would shift from prevention to isolation, remediation and recovery until the incident has been fully addressed. Any such system failures or security breaches could have a material adverse effect on the Company.

Workforce Demographic Risk

By the end of 2015, approximately 17% of the Company's employees were eligible for retirement and by the end of 2016, up to approximately 21% could be eligible. These percentages are not evenly spread across the Company's workforce, but tend to be most significant in the most senior levels of the Company's staff and especially among management staff. During each of 2015 and 2014, approximately 3% of the Company's workforce elected to retire. Accordingly, the Company's continued success will be tied to its ability to attract and retain sufficient qualified staff to replace the capability lost through retirements and to meet the demands of the Company's work programs.

In addition, the Company expects the skilled labour market for its industry to be highly competitive in the future. Many of the Company's current employees and many of the potential employees it would seek in the future possess skills and experience that would also be highly sought after by other organizations inside and outside the electricity sector. The failure to attract and retain qualified personnel for Hydro One's business could have a material adverse effect on the Company.

Labour Relations Risk

The substantial majority of the Company's employees are represented by either the Power Workers' Union or The Society of Energy Professionals. Over the past several years, significant effort has been expended to increase Hydro One's flexibility to conduct operations in a more cost efficient manner. Although the Company has achieved improved flexibility in its collective agreements, the Company may not be able to achieve further improvements. The Company recently reached an agreement with the Power Workers' Union for a renewal collective agreement with a three-year term, covering the period from April 1, 2015 to March 31, 2018 and an early renewal collective agreement with The Society of Energy Professionals with a three-year term, covering the period from April 1, 2016 to March 31, 2019. The Company also reached a renewal collective agreement with the

Canadian Union of Skilled Workers for a three-year term, covering the period from May 1, 2014 to April 30, 2017. Additionally, the Electrical Power Systems Construction Association ("EPSCA") and a number of construction unions have reached renewal agreements, to which Hydro One is bound, for a 5-year period covering May 1, 2015 to April 30, 2020. However, there can be no assurance that future collective agreement renewals with these unions or that collective agreements with the other unions with which Hydro One has contractual relationships, will be renewed on acceptable terms. The Company faces financial risks related to its ability to negotiate collective agreements consistent with its rate orders. In addition, in the event of a labour dispute, the Company could face operational risk related to continued compliance with its license requirements of providing service to customers. Any of these could have a material adverse effect on the Company.

Risk Associated with Arranging Debt Financing

The Company expects to borrow to repay its existing indebtedness and to fund a portion of capital expenditures. Hydro One Inc. has substantial amounts of existing debt, including $500 million maturing in 2016, $600 million maturing in 2017, and $750 million maturing in 2018. In addition, from time to time, the Company may draw on its syndicated bank lines and or issue short-term debt under Hydro One Inc.'s $1.5 billion commercial paper program which would need to be paid down. The Company also plans to incur capital expenditures of over $1.6 billion for each of 2016 and 2017. Cash generated from operations, after the payment of expected dividends, will not be sufficient to fund the repayment of the Company's existing indebtedness and capital expenditures. The Company's ability to arrange sufficient and cost-effective debt financing could be materially adversely affected by numerous factors, including the regulatory environment in Ontario, the Company's results of operations and financial position, market conditions, the ratings assigned to its debt securities by credit rating agencies and general economic conditions. A downgrade in the Company's credit ratings could restrict the Company's ability to access debt capital markets and increase the Company's cost of debt. Any failure or inability on the Company's part to borrow the required amounts of debt on satisfactory terms could impair its ability to repay maturing debt, fund capital expenditures and meet other obligations and requirements and, as a result, could have a material adverse effect on the Company.

Market, Financial Instrument and Credit Risk

Market risk refers primarily to the risk of loss that results from changes in costs, foreign exchange rates and interest rates. The Company is exposed to fluctuations in interest rates as its regulated return on equity is derived using a formulaic approach that takes into account anticipated interest rates, but is not currently exposed to material commodity price risk or material foreign exchange risk.

The OEB-approved adjustment formula for calculating return on equity in a deemed regulatory capital structure of 60% debt and 40% equity provides for increases and decreases depending on changes in benchmark rates of return for Government of Canada debt. The Company estimates that a 1% decrease in the forecasted long-term Government of Canada bond yield used in determining its rate of return would reduce the Company's transmission business' 2017 net income by approximately $22 million and its distribution business' 2017 net income by approximately $14 million. The Company's net income is adversely impacted by rising interest rates as the Company's maturing debt is refinanced at market rates. The Company periodically utilizes interest rate swap agreements to mitigate elements of interest rate risk.

Financial assets create a risk that a counterparty will fail to discharge an obligation, causing a financial loss. Derivative financial instruments result in exposure to credit risk, since there is a risk of counterparty default. Hydro One monitors and minimizes credit risk through various techniques, including dealing with highly-rated counterparties, limiting total exposure levels with individual counterparties, entering into master agreements which enable net settlement, and by monitoring the financial condition of counterparties. The Company does not trade in any energy derivatives. Currently, there are no significant concentrations of credit risk with respect to any class of financial assets. The Company is required to procure electricity on behalf of competitive retailers and certain local distribution companies for resale to their customers. The resulting concentrations of credit risk are mitigated through the use of various security arrangements, including letters of credit, which are incorporated into the Company's service agreements with these retailers in accordance with the OEB's Retail Settlement Code.

The failure to properly manage these risks could have a material adverse effect on the Company.

Risks Relating to Asset Condition and Capital Projects

The Company continually incurs sustainment and development capital expenditures and monitors the condition of its transmission assets to manage the risk of equipment failures and to determine the need for and timing of major refurbishments and replacements of its transmission and distribution infrastructure. However the lack of real time monitoring of distribution assets increases the risk of distribution equipment failure. The connection of large amounts of distributed generation on the distribution network has resulted in more equipment operations than in the past for the Company. This increases maintenance requirements and may accelerate the aging of the Company's assets.

Execution of the Company's capital expenditure programs, particularly for development capital expenditures, is partially dependent on external factors, such as environmental approvals, municipal permits, equipment outage schedules that accommodate the IESO, generators and transmission-connected customers, and supply chain availability for equipment suppliers and consulting services. There may also be a need for, among other things, *Environmental Assessment Act* (Ontario) approvals, approvals which require public meetings, appropriate engagement with First Nations and Métis communities, OEB approvals of expropriation or early access to property, and other activities. Obtaining approvals and carrying out these processes may also be impacted by opposition to the proposed site of the capital investments. Delays in obtaining required approvals or failure to complete capital projects on a timely basis could materially adversely affect transmission reliability or customers' service quality or increase maintenance costs which could have a material adverse effect on the Company. External factors are considered in the Company's planning process. However, if the Company is unable to carry out capital expenditure plans in a timely manner, equipment performance may degrade, which may reduce transmission capacity, compromise the reliability of the Company's transmission system or increase the costs of operating and maintaining these assets. Any of these consequences could have a material adverse effect on the Company.

Increased competition for the development of large transmission projects and legislative changes relating to the selection of transmitters could impact the Company's ability to expand its existing transmission system, which may have an adverse effect on the Company. To the extent that other parties are selected to construct, own and operate new transmission assets, the Company's share of Ontario's transmission network would be reduced.

Health, Safety and Environmental Risk

Hydro One's health, safety and environmental management system is designed to ensure hazards and risks are identified and assessed, and controls are implemented to mitigate significant risks. This system includes a standing committee of the Board of Directors that has governance over health, safety and environmental matters. However, given the expansive territory that the Company's system encompasses and the amount of equipment that it owns, the Company cannot guarantee that all such risks will be identified and mitigated without significant cost and expense to the Company. The following are some of the areas that may have a significant impact on the Company's operations.

The Company is subject to extensive Canadian federal, provincial and municipal environmental regulation. Failure to comply could subject the Company to fines or other penalties. In addition, the presence or release of hazardous or other harmful substances could lead to claims by third parties or governmental orders requiring the Company to take specific actions such as investigating, controlling and remediating the effects of these substances. Hydro One currently has a voluntary land assessment and remediation program for off-site migration in place to identify and, where necessary, remediate historical contamination that has resulted from past operational practices and uses of certain long-lasting chemicals at the Company's facilities. Any contamination of the Company's properties could limit its ability to sell or lease these assets in the future.

In addition, actual future environmental expenditures may vary materially from the estimates used in the calculation of the environmental liabilities on the Company's balance sheet. The Company does not have insurance coverage for these environmental expenditures.

There is also risk associated with obtaining governmental approvals, permits, or renewals of existing approvals and permits related to constructing or operating facilities. This may require environmental assessment or result in the imposition of conditions, or both, which could result in delays and cost increases.

Although Hydro One is not a large emitter of greenhouse gases, the Company monitors all of these emissions and has a management plan in place to track and report on all sources, including sulphur hexafluoride or "SF6". In addition, the Company recognizes the risks associated with potential climate change and has developed plans to respond as appropriate.

The Company anticipates that all of its future environmental expenditures will continue to be recoverable in future rates. However, any future regulatory decision to disallow or limit the recovery of such costs could have a material adverse effect on the Company.

Pension Plan Risk

Hydro One has the Hydro One Defined Benefit Pension Plan in place for the majority of its employees. Contributions to the pension plan are established by actuarial valuations which are minimally required to be filed with the Financial Services Commission of Ontario on a triennial basis. The most recently filed valuation was prepared as at December 31, 2013, and was filed in June 2014, covering a three year period from 2014 to 2016. Hydro One contributed approximately $174 million in respect of 2014, approximately $177 million in respect of 2015, and is expected to contribute approximately $180 million by the end of 2016 to its pension plan to satisfy minimum funding requirements. Contributions beyond 2016 are expected to continue to be significant; actual amounts will depend on investment returns, interest rates, changes in benefits and actuarial assumptions, and may include additional voluntary contributions by the Company from time to time. A determination by

the OEB that some of the Company's pension expenditures are not recoverable through rates could have a material adverse effect on the Company, and this risk may be exacerbated if the amount of required pension contributions increases.

The OEB has begun a consultation process that will examine pensions and other post-employment benefits in regulated utilities. See "– Other Post-Employment and Post-Retirement Benefits Risks". The outcome of this consultation process is uncertain and the Company is unable to assess the impact of the potential changes stemming from the review at this time.

Risk of Recoverability of Total Compensation Costs

The Company manages all of its total compensation costs, including pension and other post-employment and post-retirement benefits, subject to restrictions and requirements imposed by the collective bargaining process. Should any element of total compensation costs be disallowed in whole or part by the OEB and not be recoverable from customers in rates, the costs could be material and could lead to changes to the Company's results of operations and decrease net income, which could have a material adverse effect on the Company.

Other Post-Employment and Post-Retirement Benefits Risks

The Company provides other post-employment and post-retirement benefits, including workers compensation benefits and long-term disability benefits to qualifying employees. The OEB has begun a consultation process that will examine pensions and other post-employment benefits in regulated utilities. The objectives of the consultation are to develop standard principles to guide the OEB's review of pension and other post-employment and post-retirement benefits costs in the future, to establish specific information requirements for application and to establish appropriate regulatory mechanisms for cost recovery which can be applied consistently across the gas and electricity sectors for rate-regulated utilities. The outcome of this consultation process is uncertain and the Company is unable to assess the impact of the potential changes stemming from the review at this time. A determination that some of the Company's post-employment and post-retirement benefit costs are not recoverable could have a material adverse effect on the Company.

Risk Associated with Outsourcing Arrangements

Consistent with Hydro One's strategy of reducing operating costs, it has entered into an outsourcing arrangement with Inergi for the provision of back office services and call centre services. If the outsourcing arrangement or statements of work thereunder are terminated for any reason or expire before a new supplier is selected, the Company could be required to incur significant expenses to transfer to another service provider or insource, which could have a material adverse effect on the Company's business, operating results, financial condition or prospects.

Risk from Provincial Ownership of Transmission Corridors

The Province owns some of the corridor lands underlying the Company's transmission system. Although the Company has the statutory right to use these transmission corridors, the Company may be limited in its options to expand or operate its systems. Also, other uses of the transmission corridors by third parties in conjunction with the operation of the Company's systems may increase safety or environmental risks, which could have a material adverse effect on the Company.

Litigation Risks

In the normal course of the Company's operations, it may become involved in, be named as a party to or be the subject of, various legal proceedings, including regulatory proceedings, tax proceedings and legal actions, relating to actual or alleged violations of law, common law damages claims, personal injuries, property damage, property taxes, land rights, the environment and contract disputes. The outcome of outstanding, pending or future proceedings cannot be predicted with certainty and may be determined adversely to the Company, which could have a material adverse effect on the Company. Even if the Company prevails in any such legal proceeding, the proceedings could be costly and time-consuming and would divert the attention of management and key personnel from the Company's business operations, which could adversely affect the Company.

Risks Relating to the Company's Relationship with the Province

Ownership by the Province and Voting Power; Share Ownership Restrictions

The Province currently owns approximately 84% of the common shares of Hydro One. The *Electricity Act* restricts the Province from selling voting securities of Hydro One (including common shares) of any class or series if it would own less than 40% of the outstanding number of voting securities of that class or series after the sale and in certain circumstances also requires the Province to take steps to maintain that level of ownership. Accordingly, the Province is expected to continue to maintain a significant ownership interest in voting securities of Hydro One for an indefinite period.

As a result of its significant ownership of the common shares of Hydro One, the Province has, and is expected indefinitely to have, the ability to determine or significantly influence the outcome of shareholder votes, subject to the restrictions in the governance agreement entered into between Hydro One and the Province dated November 5, 2015 ("Governance Agreement"; available on SEDAR at www.sedar.com). While, with respect to its ownership interest in Hydro One, the Province has agreed to engage in the business and affairs of Hydro One only as an investor and not as a manager, and has stated its intention to achieve its policy objectives through legislation and regulation as it would with respect to any other utility operating in Ontario, the Governance Agreement preserves the Province's right to vote its common shares in its sole interest, which may not be aligned with the interests of the Company's other shareholders.

The share ownership restrictions in the *Electricity Act* ("Share Ownership Restrictions") and the Province's significant ownership of common shares of Hydro One together effectively prohibit one or more persons acting together from acquiring control of Hydro One. They also may limit or discourage transactions involving other fundamental changes to Hydro One and the ability of other shareholders to successfully contest the election of the directors proposed for election pursuant to the Governance Agreement. The Share Ownership Restrictions may also discourage trading in, and may limit the market for, the common shares and other voting securities.

Continued Influence by the Province

Despite the terms of the Governance Agreement in which the Province has agreed to engage in the business and affairs of the Company as an investor and not as a manager, there is a risk that the Province's engagement in the business and affairs of the Company as an investor will be informed by its own policy objectives and may influence the conduct of the business and affairs of the Company in ways that may not be aligned with the interests of other shareholders.

Nomination of Directors and Confirmation of Chief Executive Officer and Chair

Although director nominees are required to be independent of both the Company and the Province pursuant to the Governance Agreement, there is a risk that the Province will nominate or confirm individuals who satisfy the independence requirements but who it considers are disposed to support and advance its policy objectives and give disproportionate weight to the Province's interests in exercising their business judgment and balancing the interests of the stakeholders of Hydro One. This, combined with the fact certain matters require a two-thirds vote of the Board of Directors, could allow the Province to unduly influence certain Board actions such as confirmation of the Chair and confirmation of the Chief Executive Officer.

Board Removal Rights

Under the Governance Agreement, the Province has the right to withhold from voting in favour of all director nominees and has the right to seek to remove and replace the entire Board of Directors, including in each case its own director nominees but excluding the Chief Executive Officer and, at the Province's discretion, the Chair. In exercising these rights in any particular circumstance, the Province is entitled to vote in its sole interest, which may not be aligned with the interests of other shareholders.

More Extensive Regulation

Although under the Governance Agreement, the Province has agreed to engage in the business and affairs of Hydro One as an investor and not as a manager and has stated that its intention is to achieve its policy objectives through legislation and regulation as it would with respect to any other utility operating in Ontario, there is a risk that the Province will exercise its legislative and regulatory power to achieve policy objectives in a manner that has a material adverse effect on the Company.

Prohibitions on Selling the Company's Transmission or Distribution Business

The *Electricity Act* prohibits the Company from selling all or substantially all of the business, property or assets related to its transmission system or distribution system that is regulated by the OEB. There is a risk that these prohibitions may limit the ability of the Company to engage in sale transactions involving a substantial portion of either system, even where such a transaction may otherwise be considered to provide substantial benefits to the Company and the holders of the common shares.

Future Sales of Common Shares by the Province

The Province has indicated that it currently intends to sell further common shares of Hydro One over time, until it holds approximately 40% of the common shares, subject to the selling restrictions agreed with the Underwriters. The registration rights agreement between Hydro One and the Province dated November 5, 2015 (available on SEDAR at www.sedar.com) also grants the Province the right to request that Hydro One file one or more prospectuses and take other procedural steps to facilitate secondary offerings by the Province of the common shares of Hydro One. Future sales of common shares of Hydro One by the Province, or the perception that such sales could occur, may materially adversely affect market prices for these common shares and impede Hydro One's ability to raise capital through the issuance of additional common shares, including the number of common shares that Hydro One may be able to sell at a particular time or the total proceeds that may be realized.

Limitations on Enforcing the Governance Agreement

The Governance Agreement includes commitments by the Province restricting the exercise of its rights as a holder of voting securities, including with respect to the maximum number of directors that the Province may nominate and on how the Province will vote with respect to other director nominees. Hydro One's ability to obtain an effective remedy against the Province, if the Province were not to comply with these commitments, is limited as a result of the *Proceedings Against the Crown Act* (Ontario). This legislation provides that the remedies of injunction and specific performance are not available against the Province, although a court may make an order declaratory of the rights of the parties, which may influence the Province's actions. A remedy of damages would be available to Hydro One, but damages may not be an effective remedy, depending on the nature of the Province's non-compliance with the Governance Agreement.

Critical Accounting Estimates

The preparation of Hydro One Consolidated Financial Statements requires the Company to make estimates and judgments that affect the reported amounts of assets, liabilities, revenues and costs, and related disclosures of contingencies. Hydro One bases its estimates and judgments on historical experience, current conditions and various other assumptions that are believed to be reasonable under the circumstances, the results of which form the basis for making judgments about the carrying values of assets and liabilities, as well as identifying and assessing the Company's accounting treatment with respect to commitments and contingencies. Actual results may differ from these estimates and judgments. Hydro One has identified the following critical accounting estimates used in the preparation of its Consolidated Financial Statements:

Revenues

Distribution revenues are recognized on an accrual basis and include billed and unbilled revenues. Unbilled revenues are based on an estimate of electricity delivered determined by historical trends of consumption and are estimated at the end of each month. The unbilled revenue estimate is affected by energy consumption, weather, and changes in the composition of customer classes.

Accounts Receivable and Allowance for Doubtful Accounts

In 2015, the Company revised its method to estimate the unbilled accounts receivable based on new technology implemented to enhance the estimation process. This change has been accounted for on a prospective basis in the consolidated financial statements at December 31, 2015. At December 31, 2015, the change in estimate reduced unbilled accounts receivable by approximately $121 million, with a corresponding offset to various components of the retail settlement variance accounts (RSVA) regulatory asset. The change in estimate had no impact on 2015 revenues or net income.

The allowance for doubtful accounts reflects the Company's best estimate of losses on billed accounts receivable balances. The Company estimates the allowance for doubtful accounts on customer receivables by applying internally developed loss rates to the outstanding receivable balances by aging category. Loss rates applied to the accounts receivable balances are based on historical overdue balances, customer payments and write-offs.

Regulatory Assets and Liabilities

Hydro One's regulatory assets represent certain amounts receivable from future electricity customers and costs that have been deferred for accounting purposes because it is probable that they will be recovered in future rates. The regulatory assets mainly include costs related to the pension benefit liability, deferred income tax liabilities, post-retirement and post-employment benefit liability, share-based compensation costs, and environmental liabilities. The Company's regulatory liabilities represent certain amounts that are refundable to future electricity customers, and pertain primarily to OEB deferral and variance accounts. The regulatory assets and liabilities can be recognized for rate-setting and financial reporting purposes only if the amounts have been approved for inclusion in the electricity rates by the OEB, or if such approval is judged to be probable by management. If management judges that it is no longer probable that the OEB will allow the inclusion of a regulatory asset or liability in future electricity rates, the applicable carrying amount of the regulatory asset or liability will be reflected in results of operations in the period that the judgment is made by management.

Environmental Liabilities

Hydro One records a liability for the estimated future expenditures associated with the removal and destruction of PCB-contaminated insulating oils and related electrical equipment, and for the assessment and remediation of chemically-contaminated lands. There are uncertainties in estimating future environmental costs due to potential external events such as changes in legislation or regulations and advances in remediation technologies. In determining the amounts to be recorded as environmental liabilities, the Company estimates the current cost of completing required work and makes assumptions as to when the future expenditures will actually be incurred, in order to generate future cash flow information. All factors used in estimating the Company's environmental liabilities represent management's best estimates of the present value of costs required to

meet existing legislation or regulations. However, it is reasonably possible that numbers or volumes of contaminated assets, cost estimates to perform work, inflation assumptions and the assumed pattern of annual cash flows may differ significantly from the Company's current assumptions. Environmental liabilities are reviewed annually or more frequently if significant changes in regulations or other relevant factors occur. Estimate changes are accounted for prospectively.

Employee Future Benefits

Hydro One's employee future benefits consist of pension and post-retirement and post-employment plans, and include pension, group life insurance, health care, and long-term disability benefits provided to the Company's current and retired employees. Employee future benefits costs are included in Hydro One's labour costs that are either charged to results of operations or capitalized as part of the cost of property, plant and equipment and intangible assets. Changes in assumptions affect the benefit obligation of the employee future benefits and the amounts that will be charged to results of operations or capitalized in future years. The following significant assumptions and estimates are used to determine employee future benefit costs and obligations:

Weighted Average Discount Rate

The weighted average discount rate used to calculate the employee future benefits obligation is determined at each year end by referring to the most recently available market interest rates based on "AA"-rated corporate bond yields reflecting the duration of the applicable employee future benefit plan. The discount rate at December 31, 2015 remained at 4.00% for pension benefits whereas it increased to 4.10% (from 4.00% used at December 31, 2014) for the post-retirement and post-employment plans. The increase in the discount rate has resulted in a corresponding decrease in employee future benefits liabilities for the post-retirement and post-employment plans for accounting purposes. The liabilities are determined by independent actuaries using the projected benefit method prorated on service and based on assumptions that reflect management's best estimates.

Expected Rate of Return on Plan Assets

The expected rate of return on pension plan assets is based on expectations of long-term rates of return at the beginning of the year and reflects a pension asset mix consistent with the pension plan's current investment policy.

Rates of return on the respective portfolios are determined with reference to respective published market indices. The expected rate of return on pension plan assets reflects the Company's long-term expectations. We believe that this assumption is reasonable because, with the pension plan's balanced investment approach, the higher volatility of equity investment returns is intended to be offset by the greater stability of fixed-income and short-term investment returns. The net result, on a long-term basis, is a lower return than might be expected by investing in equities alone. In the short term, the pension plan can experience fluctuations in actual rates of return.

Rate of Cost of Living Increase

The rate of cost of living increase is determined by considering differences between long-term Government of Canada nominal bonds and real return bonds, which decreased from 1.70% per annum as at December 31, 2014 to approximately 1.50% per annum as at December 31, 2015. Given the Bank of Canada's commitment to keep long-term inflation between 1.00% and 3.00%, management believes that the current rate is reasonable to use as a long-term assumption and as such, has used a 2.0% per annum inflation rate for employee future benefits liability valuation purposes as at December 31, 2015.

Mortality Assumptions

The Company's employee future benefits liability is also impacted by changes in life expectancies used in mortality assumptions. Increases in life expectancies of plan members result in increases in the employee future benefits liability. The mortality assumption at December 31, 2015 is based on the final tables issued by the Canadian Institute of Actuaries (for public sector, with projection scale CPM-B and no adjustment due to pension size). This is the same assumption as was used as of December 31, 2014.

Rate of Increase in Health Care Cost Trends

The costs of post-retirement and post-employment benefits are determined at the beginning of the year and are based on assumptions for expected claims experience and future health care cost inflation. A 1% increase in the health care cost trends would result in a $22 million increase in 2015 interest cost plus service cost, and a $252 million increase in the year-end 2015 benefit liability.

Asset Impairment

Within Hydro One's regulated businesses, the carrying costs of most of the long-lived assets are included in the rate base where they earn an OEB-approved rate of return. Asset carrying values and the related return are recovered through OEB-approved rates. As a result, such assets are only tested for impairment in the event that the OEB disallows recovery, in whole or in part, or if such a disallowance is judged to be probable. We regularly monitor the assets of the

Company's unregulated Hydro One Telecom subsidiary for indications of impairment. As at December 31, 2015, no asset impairment had been recorded for assets within Hydro One's regulated or unregulated businesses.

Goodwill is evaluated for impairment on an annual basis, or more frequently if circumstances require. Hydro One has concluded that goodwill was not impaired at December 31, 2015. Goodwill represents the cost of acquired local distribution companies that is in excess of the fair value of the net identifiable assets acquired at the acquisition date.

Disclosure Controls And Internal Controls Over Financial Reporting

Internal controls have been documented and tested for adequacy and effectiveness, and continue to be refined over all business processes.

In compliance with the requirements of National Instrument 52-109, the Company's Certifying Officers have reviewed and certified the Consolidated Financial Statements for the year ended December 31, 2015, together with other financial information included in the Company's securities filings. The Certifying Officers have also certified that disclosure controls and procedures (DC&P) have been designed to provide reasonable assurance that material information relating to the Company is made known within the Company. Further, the Certifying Officers have certified that internal controls over financial reporting (ICFR) have been designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of the Consolidated Financial Statements. Based on the evaluation of the design and operating effectiveness of the Company's DC&P and ICFR, the Certifying Officers concluded that the Company's DC&P and ICFR were effective as at December 31, 2015.

New Accounting Pronouncements

In January 2015, the Financial Accounting Standards Board (FASB) issued an accounting standards update that eliminates the requirements for reporting entities to consider whether an underlying event or transaction is extraordinary and to show the item separately in the income statement. This update is applicable to Hydro One for the years and interim periods beginning on January 1, 2016. The Company does not anticipate that the adoption of this update will have a significant impact on its consolidated financial statements.

In February 2015, the FASB issued an accounting standards update that provides guidance about the analysis that a reporting entity must perform to determine whether it should consolidate certain types of legal entities. This update is applicable to Hydro One for the years and interim periods beginning on January 1, 2016. The Company does not anticipate that the adoption of this update will have a significant impact on its consolidated financial statements.

In April 2015, the FASB issued an accounting standards update that requires debt issuance costs related to a recognized debt liability to be presented on the balance sheet as a direct deduction from the carrying amount of that debt liability. The recognition and measurement guidance for debt issuance costs are not affected. This update is applicable to Hydro One for the years and interim periods beginning on January 1, 2016. Upon adoption of this update in the first quarter of 2016, the Company's deferred debt issuance costs that are currently presented under other long-term assets will be reclassified as a deduction from the carrying amount of long-term debt.

In April 2015, the FASB issued an accounting standards update that permits an entity with a fiscal year-end that does not coincide with a month-end and an entity that has a significant event in an interim period that calls for a remeasurement of defined benefit plan assets and obligations to measure the defined benefit plan assets and obligations using the month-end that is closest to the entity's fiscal year-end. This update is applicable to Hydro One for the years and interim periods beginning on January 1, 2016. The Company does not anticipate that the adoption of this update will have a significant impact on its consolidated financial statements.

In April 2015, the FASB issued an accounting standards update that provides guidance to customers about whether a cloud computing arrangement includes a software license, as well as the related accounting for the arrangement. This update is applicable to Hydro One for the years and interim periods beginning on January 1, 2016. The Company is currently assessing the impact of adoption of this update on its consolidated financial statements.

In August 2015, the FASB issued an accounting standards update that defers by one year the effective date of a revenue recognition standard issued in 2014 to January 1, 2018. The standard provides guidance on revenue recognition that depicts the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods and services. The Company is currently assessing the impact of adoption of this update on its consolidated financial statements.

In September 2015, the FASB issued an accounting standards update that requires an acquirer to recognize adjustments to provisional amounts that are identified during the measurement period of a business combination in the reporting period in which the

adjustment amounts are determined. This update is applicable to Hydro One for the years and interim periods beginning on January 1, 2016 for measurement adjustments related to business combinations.

In November 2015, the FASB issued an accounting standards update that requires all deferred tax assets and liabilities to be classified as noncurrent on the balance sheet. This update is applicable to Hydro One for the years and interim periods beginning on January 1, 2017. Upon adoption of this update in the first quarter of 2017, the current portions of the Company's deferred income tax assets and liabilities will be reclassified as long-term assets and liabilities on the consolidated Balance Sheets.

In January 2016, the FASB issued an accounting standards update that requires equity investments to be measured at fair value with changes in fair value recognized in net income, and requires enhanced disclosures and presentation of financial assets and liabilities in the financial statements. This update also simplifies the impairment assessment of equity investments without readily determinable fair values by requiring a qualitative assessment to identify impairment. This update is applicable to Hydro One for the years and interim periods beginning on January 1, 2018. The Company is currently assessing the impact of adoption of this update on its consolidated financial statements.

Other Matters

Appointment of New Board of Directors

In 2015, the Province appointed a fully independent Board of Directors to govern Hydro One as a publicly traded company, with a renewed focus on customer service excellence, improved performance and reliability, and growing shareholder value. Each of the directors, including Canadian business leaders, electricity sector experts, corporate directors and a former provincial Ombudsman, was selected based upon their independence, commercial experience, and specific expertise.

Appointment of President and Chief Executive Officer

In August 2015, the Company's Board of Directors announced the appointment of Mayo Schmidt as Hydro One's new President and Chief Executive Officer, effective September 3, 2015. Mr. Schmidt was most recently the Chief Executive Officer of Viterra Inc.

Appointment of Chief Financial Officer

In June 2015, Mr. Michael Vels was appointed to the position of Chief Financial Officer of Hydro One, effective July 1, 2015. Mr. Vels was most recently the Chief Financial Officer at Maple Leaf Foods Inc.

Appointment of Hydro One Ombudsman

In October 2015, the Hydro One Board of Directors announced the appointment of Fiona Crean to the role of Ombudsman for Hydro One, effective November 17, 2015. Ms. Crean most recently served as the City of Toronto's Ombudsman, and has worked in the area of dispute resolution and complaints investigation for more than 25 years. Ms. Crean will report directly to the Hydro One Board of Directors.

Summary of Fourth Quarter Results of Operations

Quarter ended December 31

(millions of Canadian dollars, except per share amounts)	2015	2014	Change
Revenues			
Distribution	1,148	1,268	(9.5%)
Transmission	361	382	(5.5%)
Other	13	12	8.3%
	1,522	1,662	(8.4%)
Costs			
Purchased power	786	893	(12.0%)
OM&A			
Distribution	146	148	(1.4%)
Transmission	128	86	48.8%
Other	27	13	107.7%
	301	247	21.9%
Depreciation and amortization	193	190	1.6%
	1,280	1,330	(3.8%)
Income before financing charges and income taxes	242	332	(27.1%)
Financing charges	94	98	(4.1%)
Income before income taxes	148	234	(36.8%)
Income tax expense	1	15	(93.3%)
Net income	147	219	(32.9%)
Net income attributable to common shareholders of Hydro One	143	216	(33.8%)
Basic and diluted EPS	$ 0.26	$ 0.45	(42.2%)
Capital investments			
Distribution	198	211	(6.2%)
Transmission	251	265	(5.3%)
Other	2	2	–
	451	478	(5.6%)

Net Income and EPS

The changes to net income and EPS were primarily due to the following:

- Milder weather resulted in a decrease in transmission revenues, mainly due to lower average monthly Ontario 60-minute peak demand, and lower net distribution revenues; and
- Although expenses related to stabilization of the Company's customer information system were significantly lower than last year, OM&A costs increased from last year, primarily due to:
  - expenses related to write-offs of project and inventory costs due to revisions of asset replacement strategies;
  - higher storm restoration efforts due to multiple windstorms in the fourth quarter of 2015;
  - timing of preventative maintenance on grid infrastructure;
  - insurance proceeds receipts in 2014 that did not re-occur in 2015; and
  - expenditures related to integration of acquired local distribution companies.

Income tax expense for the quarter was reduced by an income tax recovery of $19 million due to tax benefits related to the IPO.

Excluding this effect, the fourth quarter 2015 effective tax rate would have been approximately 13.8% compared to the fourth quarter 2014 effective tax rate of approximately 6.6%.

Revenues

The quarterly decrease of $21 million or 5.5% in transmission revenues was primarily due to lower average monthly Ontario 60-minute peak demand associated with unseasonably warm weather during the fourth quarter of 2015.

The quarterly decrease of $120 million or 9.5% in distribution revenues was primarily due to lower purchased power costs, the spin-off of Hydro One Brampton, and lower consumption due primarily to milder weather, partially offset by higher OEB-approved distribution rates.

OM&A Costs

The quarterly increase of $42 million or 48.8% in transmission OM&A costs was primarily due to the following:

- expenses related to write-offs of project and inventory costs due to revisions of asset replacement strategies;
- higher volumes of preventative and corrective station maintenance on power equipment;
- insurance proceeds received in the fourth quarter of 2014 related to 2013 floods at the Company's Richview and Manby transformer stations which were recorded as a reduction in 2014 OM&A costs;
- higher expenditures during 2015 related to work required to adhere to the NERC Cyber Security standards; and
- increased expenditures related to forestry control and line clearing on the Company's transmission rights-of-way.

The decrease of $2 million or 1.4% in distribution OM&A costs during the fourth quarter of 2015 was primarily due to the following:

- a decrease in bad debt expense and lower expenditures related to remediation of the Company's customer information system; and
- decreased vegetation management expenditures relating to distribution line clearing and forestry control; partially offset by
- increased costs associated with responding to power quality-related issues and outages as a result of multiple wind storms which occurred during the fourth quarter of 2015.

Depreciation and Amortization

The increase of $3 million or 1.6% in depreciation and amortization costs during the fourth quarter of 2015 compared to last year was mainly due to the growth in capital assets as the Company continues to place new assets in-service, consistent with its multi-year capital investment program.

Income Taxes

The decrease of $14 million in income tax expense for the fourth quarter of 2015 compared to 2014 was due to lower income before taxes, in addition to the positive effect of an income tax recovery associated with the step-up of the tax basis of the assets of Hydro One Inc. and its subsidiaries to fair market value in excess of the Departure Tax incurred when Hydro One exited the PILs Regime.

For the fourth quarter of 2015, the Company realized an effective tax rate of approximately 0.7%, compared to approximately 6.6% realized for the fourth quarter of 2014. The difference in the effective tax rates is due primarily to the income tax recovery on the revaluation of the assets of Hydro One on exiting the PILs Regime, partially offset by a decrease in accelerated capital cost allowance over depreciation recognized in 2014 for certain classes of assets.

Capital Investments

During the fourth quarter of 2015, the Company made capital investments totalling $451 million and placed $607 million of new assets in-service. Capital investments in the transmission system during the fourth quarter included equipment replacements at the Bruce, Richview and Pickering Transmission Stations, and continued work on the Company's major inter-area network and local area supply projects, including the Clarington Transmission Station and Guelph Area Transmission Refurbishment projects.

Capital investments in the distribution system during the fourth quarter included capital work related to station refurbishment programs and wood utility pole replacements, continued investments in new customer connections and upgrades, and increased storm restoration work as a result of two significant wind storms during the fourth quarter of 2015.

Forward-looking Statements And Information

The Company's oral and written public communications, including this document, often contain forward-looking statements that are based on current expectations, estimates, forecasts and projections about the Company's business and the industry in which it operates, and include beliefs and assumptions made by the management of the Company. Such statements include, but are not limited to: expectations regarding energy-related revenues and profit and their trend; statements regarding the Company's transmission and distribution rates resulting from rate applications; statements about

CDM; statements regarding the Company's liquidity and capital resources and operational requirements; statements about the standby credit facilities; expectations regarding the Company's financing activities; statements regarding the Company's maturing debt; statements regarding ongoing and planned projects and/or initiatives including the expected results of these projects and/or initiatives and their completion dates; expectations regarding the recoverability of large capital investments; statements regarding expected future capital and development investments, the timing of these expenditures and the Company's investment plans; statements regarding contractual obligations and other commercial commitments; statements related to the OEB; statements regarding future pension contributions, the pension plan and actuarial valuation; expectations related to workforce demographics; statements about the outsourcing arrangements with Inergi and Brookfield; expectations regarding work and costs of compliance with environmental and health and safety regulations; statements related to critical accounting estimates, including employee future benefits and expectations regarding regulatory assets and liabilities; statements about non-GAAP measures; statements regarding recent accounting-related guidance; statements about internal controls; expectations about effect of interest rates; statements related to Hydro One Brampton; statements about collective agreements; expectations regarding taxes; statements related to future sales of shares of Hydro One; statements related to the Company's relationship with the Province; statements about share-based compensation; statements related to claims; statements regarding the role of Hydro One's Ombudsman; and statements related to the Company's acquisitions and integrations, including statements about Great Lakes Power Transmission LP, Woodstock Hydro, Haldimand Hydro, and Norfolk Power. Words such as "expect", "anticipate", "intend", "attempt", "may", "plan", "will", "believe", "seek", "estimate", "goal", "aim", "target", and variations of such words and similar expressions are intended to identify such forward-looking statements. These statements are not guarantees of future performance and involve assumptions and risks and uncertainties that are difficult to predict. Therefore, actual outcomes and results may differ materially from what is expressed, implied or forecasted in such forward-looking statements. Hydro One does not intend, and it disclaims any obligation, to update any forward-looking statements, except as required by law.

These forward-looking statements are based on a variety of factors and assumptions including, but not limited to, the following: no unforeseen changes in the legislative and operating framework for Ontario's electricity market; favourable decisions from the OEB and other regulatory bodies concerning outstanding and future rate and other applications; no unexpected delays in obtaining the required approvals; no unforeseen changes in rate orders or rate setting methodologies for the Company's Distribution and Transmission Businesses; continued use of US GAAP; a stable regulatory environment; no unfavourable changes in environmental regulation; and no significant event occurring outside the ordinary course of business. These assumptions are based on information currently available to the Company, including information obtained from third party sources. Actual results may differ materially from those predicted by such forward-looking statements. While Hydro One does not know what impact any of these differences may have, the Company's business, results of operations, financial condition and credit stability may be materially adversely affected. Factors that could cause actual results or outcomes to differ materially from the results expressed or implied by forward-looking statements include, among other things:

- risks associated with the Province's significant share ownership of Hydro One and other relationships with the Province, including potential conflicts of interest that may arise between Hydro One, the Province and related parties;
- regulatory risks and risks relating to Hydro One's revenues, including risks relating to rate orders, actual performance against forecasts and capital expenditures;
- the risk that previously granted regulatory approvals may be subsequently challenged, appealed or overturned;
- the risk that the Company may be unable to comply with regulatory and legislative requirements or that the Company may incur additional costs for compliance that are not recoverable through rates;
- the risk of exposure of the Company's facilities to the effects of severe weather conditions, natural disasters or other unexpected occurrences for which the Company is uninsured or for which the Company could be subject to claims for damage;
- public opposition to and delays or denials of the requisite approvals and accommodations for the Company's planned projects;
- the risk that Hydro One may incur significant costs associated with transferring assets located on Reserves (as defined in the Indian Act (Canada));
- the risks associated with information system security and with maintaining a complex information technology system infrastructure;
- the risks related to the Company's workforce demographic and its potential inability to attract and retain qualified personnel;
- the risk of labour disputes and inability to negotiate appropriate collective agreements on acceptable terms consistent with the Company's rate decisions;
- risk that the Company is not able to arrange sufficient cost-effective financing to repay maturing debt and to fund capital expenditures;

- risks associated with fluctuations in interest rates and failure to manage exposure to credit risk;
- the risk that the Company may not be able to execute plans for capital projects necessary to maintain the performance of the Company's assets or to carry out projects in a timely manner;
- the risk of non-compliance with environmental regulations or failure to mitigate significant health and safety risks and inability to recover environmental expenditures in rate applications;
- the risk that assumptions that form the basis of the Company's recorded environmental liabilities and related regulatory assets may change;
- changes in benefits and changes in actuarial assumptions;
- the risk of not being able to recover the Company's pension expenditures in future rates and uncertainty regarding the future regulatory treatment of pension, other post-employment benefits and post-retirement benefits costs;
- the potential that Hydro One may incur significant expenses to replace some or all of the functions currently outsourced if either of the Company's agreements with Inergi or Brookfield are terminated or expire before a new service provider is selected;
- the risks associated with economic uncertainty and financial market volatility;
- the inability to prepare financial statements using US GAAP; and
- the impact of the ownership by the Province of lands underlying the Company's transmission system.

Hydro One cautions the reader that the above list of factors is not exhaustive. Some of these and other factors are discussed in more detail in the section "Risk Management and Risk Factors" in this MD&A.

In addition, Hydro One cautions the reader that information provided in this MD&A regarding the Company's outlook on certain matters, including potential future expenditures, is provided in order to give context to the nature of some of the Company's future plans and may not be appropriate for other purposes.

Additional information about Hydro One is available on SEDAR at www.sedar.com.

Management's Report

The Consolidated Financial Statements, Management's Discussion and Analysis (MD&A) and related financial information have been prepared by the management of Hydro One Limited (Hydro One or the Company). Management is responsible for the integrity, consistency and reliability of all such information presented. The Consolidated Financial Statements have been prepared in accordance with United States Generally Accepted Accounting Principles and applicable securities legislation. The MD&A has been prepared in accordance with National Instrument 51-102.

The preparation of the Consolidated Financial Statements and information in the MD&A involves the use of estimates and assumptions based on management's judgment, particularly when transactions affecting the current accounting period cannot be finalized with certainty until future periods. Estimates and assumptions are based on historical experience, current conditions and various other assumptions believed to be reasonable in the circumstances, with critical analysis of the significant accounting policies followed by the Company as described in Note 2 to the Consolidated Financial Statements. The preparation of the Consolidated Financial Statements and the MD&A includes information regarding the estimated impact of future events and transactions. The MD&A also includes information regarding sources of liquidity and capital resources, operating trends, risks and uncertainties. Actual results in the future may differ materially from the present assessment of this information because future events and circumstances may not occur as expected. The Consolidated Financial Statements and MD&A have been properly prepared within reasonable limits of materiality and in light of information up to February 11, 2016.

Management is responsible for establishing and maintaining adequate internal control over financial reporting for the Company. In meeting its responsibility for the reliability of financial information, management maintains and relies on a comprehensive system of internal control and internal audit. The system of internal control includes a written corporate conduct policy; implementation of a risk management framework; effective segregation of duties and delegation of authorities; and sound and conservative accounting policies that are regularly reviewed. This structure is designed to provide reasonable assurance that assets are safeguarded and that reliable information is available on a timely basis. In addition, management has assessed the design and operating effectiveness of the Company's internal control over financial reporting in accordance with the criteria set forth in Internal Control – Integrated Framework (2013), issued by the Committee of Sponsoring Organizations of the Treadway Commission. Based on this assessment, management concluded that the Company maintained effective internal control over financial reporting as of December 31, 2015. The effectiveness of these internal controls is reported to the Audit Committee of the Hydro One Board of Directors, as required.

The Consolidated Financial Statements have been audited by KPMG LLP, independent external auditors appointed by the shareholders of the Company. The external auditors' responsibility is to express their opinion on whether the Consolidated Financial Statements are fairly presented in accordance with United States Generally Accepted Accounting Principles. The Independent Auditors' Report outlines the scope of their examination and their opinion.

The Hydro One Board of Directors, through its Audit Committee, is responsible for ensuring that management fulfills its responsibilities for financial reporting and internal controls. The Audit Committee of Hydro One met periodically with management, the internal auditors and the external auditors to satisfy itself that each group had properly discharged its respective responsibility and to review the Consolidated Financial Statements before recommending approval by the Board of Directors. The external auditors had direct and full access to the Audit Committee, with and without the presence of management, to discuss their audit findings.

The President and Chief Executive Officer and the Chief Financial Officer have certified Hydro One's annual Consolidated Financial Statements and annual MD&A, related disclosure controls and procedures and the design and effectiveness of related internal controls over financial reporting.

On behalf of Hydro One's management:

Mayo Schmidt
President and Chief Executive Officer

Michael Vels
Chief Financial Officer

Independent Auditors' Report

To the Shareholders of Hydro One Limited

We have audited the accompanying Consolidated Financial Statements of Hydro One Limited, which comprise the consolidated balance sheets as at December 31, 2015 and December 31, 2014, the consolidated statements of operations and comprehensive income, changes in equity and cash flows for the years then ended, and notes, comprising a summary of significant accounting policies and other explanatory information.

Management's Responsibility for the Consolidated Financial Statements

Management is responsible for the preparation and fair presentation of these Consolidated Financial Statements in accordance with United States Generally Accepted Accounting Principles, and for such internal control as management determines is necessary to enable the preparation of Consolidated Financial Statements that are free from material misstatement, whether due to fraud or error.

Auditors' Responsibility

Our responsibility is to express an opinion on these Consolidated Financial Statements based on our audits. We conducted our audits in accordance with Canadian generally accepted auditing standards. Those standards require that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance about whether the Consolidated Financial Statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the Consolidated Financial Statements. The procedures selected depend on our judgment, including the assessment of the risks of material misstatement of the Consolidated Financial Statements, whether due to fraud or error. In making those risk assessments, we consider internal control relevant to the entity's preparation and fair presentation of the Consolidated Financial Statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the Consolidated Financial Statements.

We believe that the audit evidence we have obtained in our audits is sufficient and appropriate to provide a basis for our audit opinion.

Opinion

In our opinion, the Consolidated Financial Statements present fairly, in all material respects, the consolidated financial position of Hydro One Limited as at December 31, 2015 and December 31, 2014, and its consolidated results of operations and its consolidated cash flows for the years then ended in accordance with United States Generally Accepted Accounting Principles.

KPMG LLP

Chartered Professional Accountants, Licensed Public Accountants

Toronto, Canada
February 11, 2016

Consolidated Statements of Operations and Comprehensive Income

For the years ended December 31, 2015 and 2014

Year ended December 31 (millions of Canadian dollars, except per share amounts)	2015	2014
Revenues		
Distribution (includes $159 related party revenues; 2014 – $159) *(Note 23)*	4,949	4,903
Transmission (includes $1,554 related party revenues; 2014 – $1,567) *(Note 23)*	1,536	1,588
Other	53	57
	6,538	6,548
Costs		
Purchased power (includes $2,335 related party costs; 2014 – $2,633) *(Note 23)*	3,450	3,419
Operation, maintenance and administration *(Note 23)*	1,135	1,192
Depreciation and amortization *(Note 5)*	759	722
	5,344	5,333
Income before financing charges and income taxes	1,194	1,215
Financing charges *(Note 6)*	376	379
Income before income taxes	818	836
Income taxes *(Notes 7, 23)*	105	89
Net income	713	747
Other comprehensive income	1	
Comprehensive income	714	747
Net income attributable to:		
Noncontrolling interest *(Note 22)*	10	(2)
Preferred shareholders	13	18
Common shareholders	690	731
	713	747
Comprehensive income attributable to:		
Noncontrolling interest *(Note 22)*	10	(2)
Preferred shareholders	13	18
Common shareholders	691	731
	714	747
Earnings per common share *(Note 20)*		
Basic	$ 1.39	$ 1.53
Diluted	$ 1.39	$ 1.53
Dividends per common share declared *(Note 19)*	$ 1.83	$ 0.56

See accompanying notes to Consolidated Financial Statements.

Consolidated Balance Sheets

At December 31, 2015 and 2014

December 31 (millions of Canadian dollars)	2015	2014
Assets		
Current assets:		
Cash and cash equivalents *(Note 13)*	94	100
Accounts receivable (net of allowance for doubtful accounts – $61; 2014 – $66) *(Note 8)*	776	1,016
Due from related parties *(Note 23)*	191	224
Regulatory assets *(Note 11)*	36	31
Materials and supplies	21	23
Deferred income tax assets *(Note 7)*	19	19
Derivative instruments *(Note 13)*	–	2
Prepaid expenses and other assets	29	35
	1,166	1,450
Property, plant and equipment *(Note 9)*:		
Property, plant and equipment in service	26,070	25,356
Less: accumulated depreciation	9,414	9,134
	16,656	16,222
Construction in progress	1,155	1,025
Future use land, components and spares	157	154
	17,968	17,401
Other long-term assets:		
Regulatory assets *(Note 11)*	3,015	3,200
Deferred income tax assets *(Note 7)*	1,636	7
Intangible assets (net of accumulated amortization – $274; 2014 – $305) *(Note 10)*	336	276
Goodwill *(Note 4)*	163	173
Deferred debt issuance costs	34	36
Derivative instruments *(Note 13)*	1	–
Other	9	7
	5,194	3,699
Total assets	24,328	22,550

See accompanying notes to Consolidated Financial Statements.

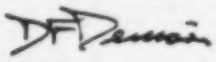
Consolidated Balance Sheets (continued)

At December 31, 2015 and 2014

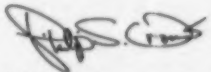
December 31 (millions of Canadian dollars, except number of shares)	2015	2014
Liabilities		
Current liabilities:		
Bank indebtedness *(Note 13)*	–	2
Short-term notes payable *(Notes 12, 13)*	1,491	–
Accounts payable	155	173
Accrued liabilities *(Notes 15, 16)*	598	611
Due to related parties *(Note 23)*	138	227
Accrued interest	96	100
Regulatory liabilities *(Note 11)*	19	47
Derivative instruments *(Note 13)*	–	3
Long-term debt payable within one year (includes $nil measured at fair value; 2014 – $252) *(Notes 12, 13)*	500	552
	2,997	1,715
Long-term debt (includes $51 measured at fair value; 2014 – $nil) *(Notes 12, 13)*	8,224	8,373
Other long-term liabilities:		
Post-retirement and post-employment benefit liability *(Note 15)*	1,560	1,533
Pension benefit liability *(Note 15)*	952	1,236
Regulatory liabilities *(Note 11)*	236	168
Deferred income tax liabilities *(Note 7)*	207	1,313
Environmental liabilities *(Note 16)*	185	221
Net unamortized debt premiums	17	18
Asset retirement obligations *(Note 17)*	9	9
Long-term accounts payable and other liabilities	17	17
	3,183	4,515
Total liabilities	14,404	14,603
Contingencies and Commitments (Notes 25, 26)		
Subsequent Events (Note 28)		
Preferred shares *(Notes 18, 19)*	–	323
Noncontrolling interest subject to redemption *(Note 22)*	23	21
Equity		
Common shares *(Notes 18, 19)*	5,623	3,314
Preferred shares *(Notes 18, 19)*	418	–
Additional paid-in capital *(Note 21)*	10	–
Retained earnings	3,806	4,249
Accumulated other comprehensive loss	(8)	(9)
Total Hydro One shareholders' equity	9,849	7,554
Noncontrolling interest *(Note 22)*	52	49
Total equity	9,901	7,603
	24,328	22,550

See accompanying notes to Consolidated Financial Statements.

On behalf of the Board of Directors:



David Denison
Chair



Philip Orsino
Chair, Audit Committee

Consolidated Statements of Changes in Equity

For the years ended December 31, 2015 and 2014

Year ended December 31, 2015 *(millions of Canadian dollars)*	Common Shares	Preferred Shares	Additional Paid-in Capital	Retained Earnings	Accumulated Other Comprehensive Loss	Total Hydro One Shareholders' Equity	Non-controlling Interest *(Note 22)*	Total Equity
January 1, 2015	3,314	–	–	4,249	(9)	7,554	49	7,603
Net income	–	–	–	703	–	703	7	710
Other comprehensive income	–	–	–	–	1	1	–	1
Distributions to noncontrolling interest	–	–	–	–	–	–	(4)	(4)
Dividends on preferred shares	–	–	–	(13)	–	(13)	–	(13)
Dividends on common shares	–	–	–	(875)	–	(875)	–	(875)
Hydro One Brampton spin-off *(Note 4)*	(196)	–	–	(258)	–	(454)	–	(454)
Pre-IPO Transactions *(Notes 1, 18)*	2,505	418	–	–	–	2,923	–	2,923
Stock-based compensation *(Note 21)*	–	–	10	–	–	10	–	10
December 31, 2015	**5,623**	**418**	**10**	**3,806**	**(8)**	**9,849**	**52**	**9,901**

Year ended December 31, 2014 *(millions of Canadian dollars)*	Common Shares	Preferred Shares	Additional Paid-in Capital	Retained Earnings	Accumulated Other Comprehensive Loss	Total Hydro One Shareholders' Equity	Non-controlling Interest *(Note 22)*	Total Equity
January 1, 2014	3,314	–	–	3,787	(9)	7,092	–	7,092
Net income	–	–	–	749	–	749	(1)	748
Other comprehensive income	–	–	–	–	–	–	–	–
Amount contributed by noncontrolling interest	–	–	–	–	–	–	50	50
Dividends on preferred shares	–	–	–	(18)	–	(18)	–	(18)
Dividends on common shares	–	–	–	(269)	–	(269)	–	(269)
December 31, 2014	3,314	–	–	4,249	(9)	7,554	49	7,603

See accompanying notes to Consolidated Financial Statements.

Consolidated Statements of Cash Flows

For the years ended December 31, 2015 and 2014

Year ended December 31 (millions of Canadian dollars)	2015	2014
Operating activities		
Net income	713	747
Environmental expenditures	(19)	(18)
Adjustments for non-cash items:		
Depreciation and amortization (excluding removal costs)	668	641
Regulatory assets and liabilities	(3)	(69)
Deferred income taxes *(Note 7)*	(2,844)	10
Other	24	–
Changes in non-cash balances related to operations *(Note 24)*	208	(55)
Net cash from (used in) operating activities	(1,253)	1,256
Financing activities		
Long-term debt issued	350	628
Long-term debt retired	(585)	(776)
Short-term notes issued	1,491	–
Common shares issued	2,600	–
Dividends paid	(888)	(287)
Amount contributed by noncontrolling interest *(Note 22)*	–	72
Distributions paid to noncontrolling interest	(5)	–
Change in bank indebtedness	(2)	(29)
Other	(7)	(3)
Net cash from (used in) financing activities	2,954	(395)
Investing activities		
Capital expenditures *(Note 24)*		
Property, plant and equipment	(1,595)	(1,481)
Intangible assets	(37)	(23)
Capital contributions received *(Note 24)*	62	–
Acquisition of Haldimand Hydro *(Note 4)*	(66)	–
Acquisition of Woodstock Hydro *(Note 4)*	(24)	–
Investment in Hydro One Brampton *(Note 4)*	(53)	–
Acquisition of Norfolk Power *(Note 4)*	–	(66)
Proceeds from investment	–	250
Other	6	(6)
Net cash used in investing activities	(1,707)	(1,326)
Net change in cash and cash equivalents	(6)	(465)
Cash and cash equivalents, beginning of year	100	565
Cash and cash equivalents, end of year	94	100

See accompanying notes to Consolidated Financial Statements.

Notes to Consolidated Financial Statements

For the years ended December 31, 2015 and 2014

1. Description of The Business

Hydro One Limited (Hydro One or the Company) was incorporated on August 31, 2015, under the *Business Corporations Act* (Ontario).

On October 31, 2015, the Company acquired Hydro One Inc., a company previously wholly-owned by the Province of Ontario (Province). The acquisition of Hydro One Inc. by Hydro One was accounted for as a common control transaction and Hydro One is a continuation of business operations of Hydro One Inc. The principal businesses of Hydro One are the transmission and distribution of electricity to customers within Ontario.

In November 2015, Hydro One and the Province completed an initial public offering (IPO) on the Toronto Stock Exchange of 15% of its 595 million outstanding common shares. The proceeds of the offering were received by the Province. All of the regulated business and outstanding publicly issued notes and debentures of Hydro One remain at the Company's wholly owned subsidiary Hydro One Inc. At December 31, 2015, the Province owns 84% of Hydro One. See Note 18 for further details regarding the reorganization of Hydro One.

2. Significant Accounting Policies

Basis of Consolidation and Preparation

These Consolidated Financial Statements have been presented in a manner similar to the pooling-of-interests method. The financial statements consist of the results of operations of Hydro One Inc. prior to October 31, 2015, and the consolidated results of operations of Hydro One from the date of incorporation on August 31, 2015 to December 31, 2015, which include the results of Hydro One Inc. subsequent to its acquisition on October 31, 2015. All periods have been combined using historical amounts. The comparative information consists of the results of Hydro One Inc. as at and for the year ended December 31, 2014. In addition, Hydro One's issued and outstanding common shares prior to October 31, 2015 have been retroactively adjusted for the purposes of presentation to reflect the effects of the acquisition of Hydro One Inc. using the exchange ratio established for the acquisition. The accompanying combined consolidated and consolidated financial statements are referred to as "consolidated" for all periods presented. Intercompany transactions and balances have been eliminated.

On August 31, 2015, Hydro One Inc. completed the spin-off of its subsidiary, Hydro One Brampton Networks Inc. (Hydro One Brampton) to the Province. See note 4 – Business Combinations. These Consolidated Financial Statements include the results of operations of Hydro One Brampton up to August 31, 2015.

Basis of Accounting

These Consolidated Financial Statements are prepared and presented in accordance with United States (US) Generally Accepted Accounting Principles (GAAP) and in Canadian dollars.

Hydro One performed an evaluation of subsequent events through to February 11, 2016, the date these Consolidated Financial Statements were issued, to determine whether any events or transactions warranted recognition and disclosure in these Consolidated Financial Statements. See Note 28 – Subsequent Events.

Use of Management Estimates

The preparation of financial statements requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities at the date of the financial statements and the reported amounts of revenues, expenses, gains and losses during the reporting periods. Management evaluates these estimates on an ongoing basis based upon historical experience, current conditions, and assumptions believed to be reasonable at the time the assumptions are made, with any adjustments being recognized in results of operations in the period they arise. Significant estimates relate to regulatory assets and regulatory liabilities, environmental liabilities, pension benefits, post-retirement and post-employment benefits; asset retirement obligations, goodwill and asset impairments, contingencies, unbilled revenues, allowance for doubtful accounts, derivative instruments, and deferred income tax assets and liabilities. Actual results may differ significantly from these estimates.

Rate Setting

The Company's Transmission Business consists of the transmission business of Hydro One Inc., which includes the transmission business of its subsidiary, Hydro One Networks Inc. (Hydro One Networks), as well as its 66% interest in B2M Limited Partnership (B2M LP). The

Company's Distribution Business consists of the distribution business of Hydro One Inc., which includes the distribution businesses of Hydro One Networks, Haldimand County Utilities Inc. (Haldimand Hydro), Hydro One Remote Communities Inc. (Hydro One Remote Communities), and Woodstock Hydro Holdings Inc. (Woodstock Hydro).

The Ontario Energy Board (OEB) has approved the use of US GAAP for rate setting and regulatory accounting and reporting by Hydro One Networks' transmission and distribution businesses, as well as by Hydro One Remote Communities.

Transmission

On January 8, 2015, pursuant to an application filed with the OEB, the OEB approved the 2015 Hydro One transmission rates revenue requirement, excluding the B2M LP revenue requirement, of $1,477 million.

On June 30, 2015, B2M LP updated its application (originally filed March 30, 2015) with the OEB for 2015-2019 transmission rates, requesting approval of revenue requirement of $39 million, $36 million, $37 million, $38 million and $37 million for the respective years. On December 29, 2015, the OEB issued a Decision and Order approving the 2015-2019 rates revenue requirement, and on January 14, 2016, the OEB approved the B2M LP revenue requirement recovery through the 2016 Uniform Transmission Rates, and the establishment of a deferral account to capture costs of Tax Rate and Rule changes.

Distribution

On March 12, 2015, the OEB issued a Decision and Rate Order approving a revenue requirement of $1,326 million for 2015, $1,430 million for 2016 and $1,486 million for 2017. The revenue requirements for 2016 and 2017 are estimates that may change based on 2016 and 2017 Rate Orders. On April 23, 2015, the Final Rate Order for 2015 rates was approved by the OEB.

On September 24, 2014, Hydro One Remote Communities filed an Incentive Regulation Mechanism application with the OEB for 2015 rates, seeking approval for increased base rates for the distribution and generation of electricity of 1.7%. On March 19, 2015, the OEB approved an increase of approximately 1.6% to basic rates for the distribution and generation of electricity, with an effective date of May 1, 2015.

Regulatory Accounting

The OEB has the general power to include or exclude revenues, costs, gains or losses in the rates of a specific period, resulting in a change in the timing of accounting recognition from that which would have been applied in an unregulated company. Such change in timing involves the application of rate-regulated accounting, giving rise to the recognition of regulatory assets and liabilities. The Company's regulatory assets represent certain amounts receivable from future customers and costs that have been deferred for accounting purposes because it is probable that they will be recovered in future rates. In addition, the Company has recorded regulatory liabilities that generally represent amounts that are refundable to future customers. The Company continually assesses the likelihood of recovery of each of its regulatory assets and continues to believe that it is probable that the OEB will factor its regulatory assets and liabilities into the setting of future rates. If, at some future date, the Company judges that it is no longer probable that the OEB will include a regulatory asset or liability in setting future rates, the appropriate carrying amount will be reflected in results of operations in the period that the assessment is made.

Cash and Cash Equivalents

Cash and cash equivalents include cash and short-term investments with an original maturity of three months or less.

Revenue Recognition

Transmission revenues are collected through OEB-approved rates, which are based on an approved revenue requirement that includes a rate of return. Such revenue is recognized as electricity is transmitted and delivered to customers.

Distribution revenues attributable to the delivery of electricity are based on OEB-approved distribution rates and are recognized on an accrual basis and include billed and unbilled revenues. Billed revenues are based on electricity delivered as measured from customer meters. Unbilled revenues are based on an estimate of electricity delivered determined by historical trends of consumption and are estimated at the end of each month. The unbilled revenue estimate is affected by energy consumption, weather, and changes in the composition of customer classes.

Distribution revenue also includes an amount relating to rate protection for rural, residential and remote customers, which is received from the Independent Electricity System Operator (IESO) based on a standardized customer rate that is approved by the OEB.

Revenues also include amounts related to sales of other services and equipment. Such revenue is recognized as services are rendered or as equipment is delivered.

Revenues are recorded net of indirect taxes.

Accounts Receivable and Allowance for Doubtful Accounts

Billed accounts receivable are recorded at the invoiced amount, net of allowance for doubtful accounts. Unbilled accounts receivable are recorded at their estimated value. Overdue amounts related to regulated billings bear interest at OEB-approved rates. The allowance for doubtful accounts reflects the Company's best estimate of losses on billed accounts receivable balances. The Company estimates the allowance for doubtful accounts on customer receivables by applying internally developed loss rates to the outstanding receivable balances by aging category. Loss rates applied to the accounts receivable balances are based on historical overdue balances, customer payments and write-offs. Accounts receivable are written-off against the allowance when they are deemed uncollectible. The existing allowance for doubtful accounts will continue to be affected by changes in volume, prices and economic conditions.

Noncontrolling interest

Noncontrolling interest represents the portion of equity ownership in subsidiaries that is not attributable to shareholders of Hydro One. Noncontrolling interest is initially recorded at fair value and subsequently the amount is adjusted for the proportionate share of net income (loss) and other comprehensive income (loss) attributable to the noncontrolling interest and any dividends or distributions paid to the noncontrolling interest.

If a transaction results in the acquisition of all, or part, of a noncontrolling interest in a subsidiary, the acquisition of the noncontrolling interest is accounted for as an equity transaction. No gain or loss is recognized in consolidated net income or comprehensive income as a result of changes in the noncontrolling interest, unless a change results in the loss of control by the Company.

Income Taxes

By virtue of being wholly owned by the Province, Hydro One was exempt from tax under the *Income Tax Act* (Canada) and the *Taxation Act, 2007* (Ontario) (Federal Tax Regime). However, under the *Electricity Act*, Hydro One was required to make payments in lieu of tax (PILs) to the Ontario Electricity Financial Corporation (OEFC) (PILs Regime). The PILs were, in general, based on the amount of tax that Hydro One would otherwise be liable to pay under the Federal Tax Regime if it was not exempt from taxes under those statutes.

In connection with the IPO of Hydro One, Hydro One's exemption from tax under the Federal Tax Regime ceased to apply. Upon exiting the PILs Regime, Hydro One is required to make corporate income tax payments to the Canada Revenue Agency (CRA) under the Federal Tax Regime.

Current and deferred income taxes are computed based on the tax rates and tax laws enacted as at the balance sheet date. Tax benefits associated with income tax positions taken, or expected to be taken, in a tax return are recorded only when the "more-likely-than-not" recognition threshold is satisfied and are measured at the largest amount of benefit that has a greater than 50% likelihood of being realized upon settlement. Management evaluates each position based solely on the technical merits and facts and circumstances of the position, assuming the position will be examined by a taxing authority having full knowledge of all relevant information. Significant management judgment is required to determine recognition thresholds and the related amount of tax benefits to be recognized in the Consolidated Financial Statements. Management re-evaluates tax positions each period in which new information about recognition or measurement becomes available.

Deferred Income Taxes

Deferred income taxes are provided for using the liability method. Deferred income taxes are recognized based on the estimated future tax consequences attributable to temporary differences between the carrying amount of assets and liabilities in the Consolidated Financial Statements and their corresponding tax bases.

Deferred income tax liabilities are generally recognized on all taxable temporary differences. Deferred tax assets are recognized to the extent that it is more-likely-than-not that these assets will be realized from taxable income available against which deductible temporary differences can be utilized.

Deferred income taxes are calculated at the tax rates that are expected to apply in the period when the liability is settled or the asset is realized, based on the tax rates and tax laws that have been enacted as at the balance sheet date. Deferred income taxes that are not included in the rate-setting process are charged or credited to the Consolidated Statements of Operations and Comprehensive Income.

If management determines that it is more-likely-than-not that some or all of a deferred income tax asset will not be realized, a valuation allowance is recorded against the deferred income tax asset to report the net balance at the amount expected to be realized. Previously unrecognized deferred income tax assets are reassessed at each balance sheet date and are recognized to the extent that it has become more-likely-than-not that the tax benefit will be realized.

The Company records regulatory assets and liabilities associated with deferred income taxes that will be included in the rate-setting process.

The Company uses the flow-through method to account for investment tax credits (ITCs) earned on eligible scientific research and experimental development expenditures, and apprenticeship job

creation. Under this method, only non-refundable ITCs are recognized as a reduction to income tax expense.

Materials and Supplies

Materials and supplies represent consumables, small spare parts and construction materials held for internal construction and maintenance of property, plant and equipment. These assets are carried at average cost less any impairments recorded.

Property, Plant and Equipment

Property, plant and equipment is recorded at original cost, net of customer contributions, and any accumulated impairment losses. The cost of additions, including betterments and replacement asset components, is included on the Consolidated Balance Sheets as property, plant and equipment.

The original cost of property, plant and equipment includes direct materials, direct labour (including employee benefits), contracted services, attributable capitalized financing costs, asset retirement costs, and direct and indirect overheads that are related to the capital project or program. Indirect overheads include a portion of corporate costs such as finance, treasury, human resources, information technology and executive costs. Overhead costs, including corporate functions and field services costs, are capitalized on a fully allocated basis, consistent with an OEB-approved methodology.

Property, plant and equipment in service consists of transmission, distribution, communication, administration and service assets and land easements. Property, plant and equipment also includes future use assets, such as land, major components and spare parts, and capitalized project development costs associated with deferred capital projects.

Transmission

Transmission assets include assets used for the transmission of high-voltage electricity, such as transmission lines, support structures, foundations, insulators, connecting hardware and grounding systems, and assets used to step up the voltage of electricity from generating stations for transmission and to step down voltages for distribution, including transformers, circuit breakers and switches.

Distribution

Distribution assets include assets related to the distribution of low-voltage electricity, including lines, poles, switches, transformers, protective devices and metering systems.

Communication

Communication assets include fibre optic and microwave radio systems, optical ground wire, towers, telephone equipment and associated buildings.

Administration and Service

Administration and service assets include administrative buildings, personal computers, transport and work equipment, tools and other minor assets.

Easements

Easements include statutory rights of use for transmission corridors and abutting lands granted under the *Reliable Energy and Consumer Protection Act, 2002*, as well as other land access rights.

Intangible Assets

Intangible assets separately acquired or internally developed are measured on initial recognition at cost, which comprises purchased software, direct labour (including employee benefits), consulting, engineering, overheads and attributable capitalized financing charges. Following initial recognition, intangible assets are carried at cost, net of any accumulated amortization and accumulated impairment losses. The Company's intangible assets primarily represent major computer applications.

Capitalized Financing Costs

Capitalized financing costs represent interest costs attributable to the construction of property, plant and equipment or development of intangible assets. The financing cost of attributable borrowed funds is capitalized as part of the acquisition cost of such assets. The capitalized financing costs are a reduction of financing charges recognized in the Consolidated Statements of Operations and Comprehensive Income. Capitalized financing costs are calculated using the Company's weighted average effective cost of debt.

Construction and Development in Progress

Construction and development in progress consists of the capitalized cost of constructed assets that are not yet complete and which have not yet been placed in service.

Depreciation and Amortization

The cost of property, plant and equipment and intangible assets is depreciated or amortized on a straight-line basis based on the estimated remaining service life of each asset category, except for transport and work equipment, which is depreciated on a declining balance basis.

The Company periodically initiates an external independent review of its property, plant and equipment and intangible asset depreciation and amortization rates, as required by the OEB. Any changes arising from OEB approval of such a review are implemented on a remaining service life basis, consistent with their inclusion in electricity rates. The last review resulted in changes to rates effective January 1, 2015. A summary of average service lives and depreciation and amortization rates for the various classes of assets is included below:

	Average Service Life	Rate Range	Rate Average
Transmission	56 years	1% – 2%	2%
Distribution	46 years	1% – 7%	2%
Communication	16 years	1% – 15%	6%
Administration and service	18 years	1% – 20%	6%

The cost of intangible assets is included primarily within the administration and service classification above. Amortization rate for computer applications software and other intangible assets is 10%.

In accordance with group depreciation practices, the original cost of property, plant and equipment, or major components thereof, and intangible assets that are normally retired, is charged to accumulated depreciation, with no gain or loss being reflected in results of operations. Where a disposition of property, plant and equipment occurs through sale, a gain or loss is calculated based on proceeds and such gain or loss is included in depreciation expense. Depreciation expense also includes the costs incurred to remove property, plant and equipment where no asset retirement obligations have been recorded.

Goodwill

Goodwill represents the cost of acquired local distribution companies that is in excess of the fair value of the net identifiable assets acquired at the acquisition date. Goodwill is not included in rate base.

Goodwill is evaluated for impairment on an annual basis, or more frequently if circumstances require. The Company performs a qualitative assessment to determine whether it is more-likely-than-not that the fair value of the applicable reporting unit is less than its carrying amount. If the Company determines, as a result of its qualitative assessment, that it is not more-likely-than-not that the fair value of the applicable reporting unit is less than its carrying amount, no further testing is required. If the Company determines, as a result of its qualitative assessment, that it is more-likely-than-not that the fair value of the applicable reporting unit is less than its carrying amount, a goodwill impairment assessment is performed using a two-step, fair value-based test. The first step compares the fair value of the applicable reporting unit to its carrying amount, including goodwill. If the carrying amount of the applicable reporting unit exceeds its fair value, a second step is performed. The second step requires an allocation of fair value to the individual assets and liabilities using purchase price allocation in order to determine the implied fair value of goodwill. If the implied fair value of goodwill is less than the carrying amount, an impairment loss is recorded as a reduction to goodwill and as a charge to results of operations.

For the year ended December 31, 2015, based on the qualitative assessment performed as at September 30, 2015, the Company has determined that it is not more-likely-than-not that the fair value of each applicable reporting unit assessed is less than its carrying amount. As a result, no further testing was performed, and the Company has concluded that goodwill was not impaired at December 31, 2015.

Long-Lived Asset Impairment

When circumstances indicate the carrying value of long-lived assets may not be recoverable, the Company evaluates whether the carrying value of such assets, excluding goodwill, has been impaired. For such long-lived assets, the Company evaluates whether impairment may exist by estimating future estimated undiscounted cash flows expected to result from the use and eventual disposition of the asset. When alternative courses of action to recover the carrying amount of a long-lived asset are under consideration, a probability-weighted approach is used to develop estimates of future undiscounted cash flows. If the carrying value of the long-lived asset is not recoverable based on the estimated future undiscounted cash flows, an impairment loss is recorded, measured as the excess of the carrying value of the asset over its fair value. As a result, the asset's carrying value is adjusted to its estimated fair value.

Within its regulated business, the carrying costs of most of Hydro One's long-lived assets are included in rate base where they earn an OEB-approved rate of return. Asset carrying values and the related return are recovered through approved rates. As a result, such assets are only tested for impairment in the event that the OEB disallows recovery, in whole or in part, or if such a disallowance is judged to be probable.

Hydro One regularly monitors the assets of its unregulated Hydro One Telecom subsidiary for indications of impairment. Management

assesses the fair value of such long-lived assets using commonly accepted techniques, and may use more than one. Techniques used to determine fair value include, but are not limited to, the use of recent third party comparable sales for reference and internally developed discounted cash flow analysis. Significant changes in market conditions, changes to the condition of an asset, or a change in management's intent to utilize the asset are generally viewed by management as triggering events to reassess the cash flows related to these long-lived assets. As at December 31, 2015 and 2014, no asset impairment had been recorded for assets within either the Company's regulated or unregulated businesses.

Costs of Arranging Debt Financing

For financial liabilities classified as other than held-for-trading, the Company defers the external transaction costs related to obtaining debt financing and presents such amounts as deferred debt issuance costs on the Consolidated Balance Sheets. Deferred debt issuance costs are amortized over the contractual life of the related debt on an effective interest basis and the amortization is included within financing charges in the Consolidated Statements of Operations and Comprehensive Income. Transaction costs for items classified as held-for-trading are expensed immediately.

Comprehensive Income

Comprehensive income is comprised of net income and other comprehensive income (OCI). Hydro One presents net income and OCI in a single continuous Consolidated Statement of Operations and Comprehensive Income.

Financial Assets and Liabilities

All financial assets and liabilities are classified into one of the following five categories: held-to-maturity; loans and receivables; held-for-trading; other liabilities; or available-for-sale. Financial assets and liabilities classified as held-for-trading are measured at fair value. All other financial assets and liabilities are measured at amortized cost, except accounts receivable and amounts due from related parties, which are measured at the lower of cost or fair value. Accounts receivable and amounts due from related parties are classified as loans and receivables. The Company considers the carrying amounts of accounts receivable and amounts due from related parties to be reasonable estimates of fair value because of the short time to maturity of these instruments. Provisions for impaired accounts receivable are recognized as adjustments to the allowance for doubtful accounts and are recognized when there is objective evidence that the Company will not be able to collect amounts according to the original terms. All financial instrument transactions are recorded at trade date.

Derivative instruments are measured at fair value. Gains and losses from fair valuation are included within financing charges in the period in which they arise. The Company determines the classification of its financial assets and liabilities at the date of initial recognition. The Company designates certain of its financial assets and liabilities to be held at fair value, when it is consistent with the Company's risk management policy disclosed in Note 13 – Fair Value of Financial Instruments and Risk Management.

Derivative Instruments and Hedge Accounting

The Company closely monitors the risks associated with changes in interest rates on its operations and, where appropriate, uses various instruments to hedge these risks. Certain of these derivative instruments qualify for hedge accounting and are designated as accounting hedges, while others either do not qualify as hedges or have not been designated as hedges (hereinafter referred to as undesignated contracts) as they are part of economic hedging relationships.

The accounting guidance for derivative instruments requires the recognition of all derivative instruments not identified as meeting the normal purchase and sale exemption as either assets or liabilities recorded at fair value on the Consolidated Balance Sheets. For derivative instruments that qualify for hedge accounting, the Company may elect to designate such derivative instruments as either cash flow hedges or fair value hedges. The Company offsets fair value amounts recognized on its Consolidated Balance Sheets related to derivative instruments executed with the same counterparty under the same master netting agreement.

For derivative instruments that qualify for hedge accounting and which are designated as cash flow hedges, the effective portion of any gain or loss, net of tax, is reported as a component of accumulated OCI (AOCI) and is reclassified to results of operations in the same period or periods during which the hedged transaction affects results of operations. Any gains or losses on the derivative instrument that represent either hedge ineffectiveness or hedge components excluded from the assessment of effectiveness are recognized in results of operations. For fair value hedges, changes in fair value of both the derivative instrument and the underlying hedged exposure are recognized in the Consolidated Statements of Operations and Comprehensive Income in the current period. The gain or loss on the derivative instrument is included in the same line item as the offsetting gain or loss on the hedged item in the Consolidated Statements of Operations and Comprehensive Income. Additionally, the Company enters into derivative agreements that are economic hedges which either do not qualify for hedge accounting or have not been designated as hedges. The changes in fair value of these undesignated derivative instruments are reflected in results of operations.

Embedded derivative instruments are separated from their host contracts and carried at fair value on the Consolidated Balance Sheets when: (a) the economic characteristics and risks of the embedded derivative are not clearly and closely related to the economic characteristics and risks of the host contract; (b) the hybrid instrument is not measured at fair value, with changes in fair value recognized in results of operations each period; and (c) the embedded derivative itself meets the definition of a derivative. The Company does not engage in derivative trading or speculative activities and had no embedded derivatives at December 31, 2015 or 2014.

Hydro One periodically develops hedging strategies taking into account risk management objectives. At the inception of a hedging relationship where the Company has elected to apply hedge accounting, Hydro One formally documents the relationship between the hedged item and the hedging instrument, the related risk management objective, the nature of the specific risk exposure being hedged, and the method for assessing the effectiveness of the hedging relationship. The Company also assesses, both at the inception of the hedge and on a quarterly basis, whether the hedging instruments are effective in offsetting changes in fair values or cash flows of the hedged items.

Employee Future Benefits

Employee future benefits provided by Hydro One include pension, post-retirement and post-employment benefits. The costs of the Company's pension, post-retirement and post-employment benefit plans are recorded over the periods during which employees render service.

The Company recognizes the funded status of its defined benefit pension, post-retirement and post-employment plans on its Consolidated Balance Sheets and subsequently recognizes the changes in funded status at the end of each reporting year. Defined benefit pension, post-retirement and post-employment plans are considered to be underfunded when the projected benefit obligation exceeds the fair value of the plan assets. Liabilities are recognized on the Consolidated Balance Sheets for any net underfunded projected benefit obligation. The net underfunded projected benefit obligation may be disclosed as a current liability, long-term liability, or both. The current portion is the amount by which the actuarial present value of benefits included in the benefit obligation payable in the next 12 months exceeds the fair value of plan assets. If the fair value of plan assets exceeds the projected benefit obligation of the plan, an asset is recognized equal to the net overfunded projected benefit obligation. The post-retirement and post-employment benefit plans are unfunded because there are no related plan assets.

Pension benefits

Pension costs are recorded on an accrual basis for financial reporting purposes. Pension costs are actuarially determined using the projected benefit method prorated on service and are based on assumptions that reflect management's best estimate of the effect of future events, including future compensation increases. Past service costs from plan amendments and all actuarial gains and losses are amortized on a straight-line basis over the expected average remaining service period of active employees in the plan, and over the estimated remaining life expectancy of inactive employees in the plan. Pension plan assets, consisting primarily of listed equity securities as well as corporate and government debt securities, are fair valued at the end of each year. Hydro One records a regulatory asset equal to the net underfunded projected benefit obligation for its pension plan.

Post-retirement and post-employment benefits

Post-retirement and post-employment benefits are recorded and included in rates on an accrual basis. Costs are determined by independent actuaries using the projected benefit method prorated on service and based on assumptions that reflect management's best estimates. Past service costs from plan amendments are amortized to results of operations based on the expected average remaining service period. Hydro One records a regulatory asset equal to the incremental net unfunded projected benefit obligation for post retirement and post-employment plans recorded at each year end based on annual actuarial reports.

For post-retirement benefits, all actuarial gains or losses are deferred using the "corridor" approach. The amount calculated above the "corridor" is amortized to results of operations on a straight-line basis over the expected average remaining service life of active employees in the plan and over the remaining life expectancy of inactive employees in the plan. The post-retirement benefit obligation is remeasured to its fair value at each year end based on an annual actuarial report, with an offset to the associated regulatory asset, to the extent of the remeasurement adjustment.

For post-employment obligations, the associated regulatory liabilities representing actuarial gains on transition to US GAAP are amortized to results of operations based on the "corridor" approach. Post transition, the actuarial gains and losses on post-employment obligations that are incurred during the year are recognized immediately to results of operations. The post-employment benefit obligation is remeasured to its fair value at each year end based on an annual actuarial report, with an offset to the associated regulatory asset, to the extent of the remeasurement adjustment.

All post-retirement and post-employment future benefit costs are attributed to labour and are either charged to results of operations or capitalized as part of the cost of property, plant and equipment and intangible assets.

Multiemployer Pension Plan

Former employees of Haldimand Hydro and Woodstock Hydro participate in the Ontario Municipal Employees Retirement System Fund (OMERS Plan), a multiemployer, contributory, defined benefit public sector pension fund. Former employees of Norfolk Power Inc. (Norfolk Power) ceased to contribute to the OMERS Plan upon integration of Norfolk Power into Hydro One Networks in September 2015. These employees are now included in Hydro One's defined benefit pension plan. OMERS Plan provides retirement pension payments based on members' length of service and salary. Both the participating employers and members are required to make plan contributions. The OMERS Plan assets are pooled together to provide benefits to all plan participants and the plan assets are not segregated by member entity. The OMERS Plan is registered with the Financial Services Commission of Ontario under Registration #0345983.

The OMERS Plan is accounted for as a defined contribution plan by Hydro One because it is not practicable to determine the present value of the Company's obligation, the fair value of plan assets or the related current service cost applicable to employees of Haldimand Hydro and Woodstock Hydro. Hydro One recognizes its contributions to the OMERS Plan as pension expense, with a portion being capitalized. The expensed amount is included in operation, maintenance and administration costs in the Consolidated Statements of Operations and Comprehensive Income.

Stock-Based Compensation

Hydro One measures share grant plans based on fair value of share grants as estimated based on the grant date share price. The costs are recognized in the financial statements using the graded-vesting attribution method for share grant plans that have both a performance condition and a service condition. The Company records a regulatory asset equal to the accrued costs of share grant plans recognized in each period, as management considers it to be probable that such costs will be recovered in the future through the rate-setting process.

The Company also records the liabilities associated with its Directors' Deferred Share Unit (DSU) Plan at fair value at each reporting date until settlement, recognizing compensation expense over the vesting period on a straight-line basis. The fair value of the DSU liability is based on the Company's common share closing price at the end of each reporting period.

Loss Contingencies

Hydro One is involved in certain legal and environmental matters that arise in the normal course of business. In the preparation of its Consolidated Financial Statements, management makes judgments regarding the future outcome of contingent events and records a loss for a contingency based on its best estimate when it is determined that such loss is probable and the amount of the loss can be reasonably estimated. Where the loss amount is recoverable in future rates, a regulatory asset is also recorded. When a range estimate for the probable loss exists and no amount within the range is a better estimate than any other amount, the Company records a loss at the minimum amount within the range.

Management regularly reviews current information available to determine whether recorded provisions should be adjusted and whether new provisions are required. Estimating probable losses may require analysis of multiple forecasts and scenarios that often depend on judgments about potential actions by third parties, such as federal, provincial and local courts or regulators. Contingent liabilities are often resolved over long periods of time. Amounts recorded in the Consolidated Financial Statements may differ from the actual outcome once the contingency is resolved. Such differences could have a material impact on future results of operations, financial position and cash flows of the Company.

Provisions are based upon current estimates and are subject to greater uncertainty where the projection period is lengthy. A significant upward or downward trend in the number of claims filed, the nature of the alleged injuries, and the average cost of resolving each claim could change the estimated provision, as could any substantial adverse or favourable verdict at trial. A federal or provincial legislative outcome or structured settlement could also change the estimated liability. Legal fees are expensed as incurred.

Environmental Liabilities

Environmental liabilities are recorded in respect of past contamination when it is determined that future environmental remediation expenditures are probable under existing statute or regulation and the amount of the future expenditures can be reasonably estimated. Hydro One records a liability for the estimated future expenditures associated with contaminated land assessment and remediation and for the phase-out and destruction of polychlorinated biphenyl (PCB)-contaminated mineral oil removed from electrical equipment, based on the present value of these estimated future expenditures. The Company determines the present value with a discount rate equal to its credit-adjusted risk-free interest rate on financial instruments with comparable maturities to the pattern of future environmental expenditures. As the Company anticipates that the future expenditures will continue to be recoverable in future rates, an offsetting regulatory

asset has been recorded to reflect the future recovery of these environmental expenditures from customers. Hydro One reviews its estimates of future environmental expenditures annually, or more frequently if there are indications that circumstances have changed.

Asset Retirement Obligations

Asset retirement obligations are recorded for legal obligations associated with the future removal and disposal of long-lived assets. Such obligations may result from the acquisition, construction, development and/or normal use of the asset. Conditional asset retirement obligations are recorded when there is a legal obligation to perform a future asset retirement activity but where the timing and/or method of settlement are conditional on a future event that may or may not be within the control of the Company. In such a case, the obligation to perform the asset retirement activity is unconditional even though uncertainty exists about the timing and/or method of settlement.

When recording an asset retirement obligation, the present value of the estimated future expenditures required to complete the asset retirement activity is recorded in the period in which the obligation is incurred, if a reasonable estimate can be made. In general, the present value of the estimated future expenditures is added to the carrying amount of the associated asset and the resulting asset retirement cost is depreciated over the estimated useful life of the asset. Where an asset is no longer in service when an asset retirement obligation is recorded, the asset retirement cost is recorded in results of operations.

Some of the Company's transmission and distribution assets, particularly those located on unowned easements and rights-of-way, may have asset retirement obligations, conditional or otherwise. The majority of the Company's easements and rights-of-way are either of perpetual duration or are automatically renewed annually. Land rights with finite terms are generally subject to extension or renewal. As the Company expects to use the majority of its facilities in perpetuity, no asset retirement obligations currently exist for these assets. If, at some future date, a particular facility is shown not to meet the perpetuity assumption, it will be reviewed to determine whether an estimable asset retirement obligation exists. In such a case, an asset retirement obligation would be recorded at that time.

The Company's asset retirement obligations recorded to date relate to estimated future expenditures associated with the removal and disposal of asbestos-containing materials installed in some of its facilities and with the decommissioning of specific switching stations located on unowned sites.

3. New Accounting Pronouncements

Recent Accounting Guidance Not Yet Adopted

In January 2015, the Financial Accounting Standards Board (FASB) issued Accounting Standards Update (ASU) 2015-01, Income Statement – Extraordinary and Unusual Items (Subtopic 225-20): Simplifying Income Statement Presentation by Eliminating the Concept of Extraordinary Items. This ASU eliminates the requirements for reporting entities to consider whether an underlying event or transaction is extraordinary and to show the item separately in the income statement. This ASU is effective for fiscal years, and interim periods within these years, beginning after December 15, 2015. The adoption of this ASU is not anticipated to have an impact on the Company's consolidated financial statements.

In February 2015, the FASB issued ASU 2015-02, Consolidation (Topic 810): Amendments to the Consolidation Analysis. This ASU provides guidance about the analysis that a reporting entity must perform to determine whether it should consolidate certain types of legal entities. This ASU is effective for fiscal years, and interim periods within those years, beginning after December 15, 2015. The adoption of this ASU is not anticipated to have an impact on the Company's consolidated financial statements.

In April 2015, the FASB issued ASU 2015-03, Interest – Imputation of Interest (Subtopic 835-30): Simplifying the Presentation of Debt Issuance Costs. This ASU requires that debt issuance costs related to a recognized debt liability be presented in the balance sheet as a direct deduction from the carrying amount of that debt liability. The recognition and measurement guidance for debt issuance costs are not affected. This ASU is effective for fiscal years, and interim periods within those years, beginning after December 15, 2015. Upon adoption of this ASU in the first quarter of 2016, the Company's deferred debt issuance costs that are currently presented under other long-term assets will be reclassified as a deduction from the carrying amount of long-term debt.

In April 2015, the FASB issued ASU 2015-04, Compensation – Retirement Benefits (Topic 715): Practical Expedient for the Measurement Date of an Employer's Defined Benefit Obligation and Plan Assets. This ASU permits an entity with a fiscal year-end that does not coincide with a month-end and an entity that has a significant event in an interim period that calls for a remeasurement of defined benefit plan assets and obligations to measure the defined benefit plan assets and obligations using the month-end that is closest to the entity's fiscal year-end. This ASU is effective for fiscal years, and interim periods within these years, beginning after December 15, 2015. The adoption of this ASU is not anticipated to have an impact on the Company's consolidated financial statements.

In April 2015, the FASB issued ASU 2015-05, Intangibles – Goodwill and Other – Internal-Use Software (Subtopic 350-40): Customer's Accounting for Fees Paid in a Cloud Computing Arrangement. This ASU provides guidance to customers about whether a cloud computing arrangement includes a software license, as well as the related accounting for the arrangement. This ASU is effective for fiscal years, and interim periods within these years, beginning after December 15, 2015. The Company is currently assessing the impact of adoption of this ASU on its consolidated financial statements.

In August 2015, the FASB issued ASU 2015-14, Revenue from Contracts with Customers (Topic 606): Deferral of the Effective Date. This ASU defers by one year the effective date of ASU 2014-09, Revenue from Contracts with Customers (Topic 606) issued by the FASB in May 2014. ASU 2014-09 provides guidance on revenue recognition that depicts the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods and services. The guidance in ASU 2014-09 is now effective for fiscal years, and interim periods within those years, beginning after December 15, 2017. The Company is currently assessing the impact of adoption of ASU 2014-09 on its consolidated financial statements.

In September 2015, the FASB issued ASU 2015-16, Business Combinations (Topic 805): Simplifying the Accounting for Measurement-Period Adjustments. The amendments in this ASU require that an acquirer recognize adjustments to provisional amounts that are identified during the measurement period of a business combination in the reporting period in which the adjustment amounts are determined. The amendments in this update require that the acquirer to present separately on the face of the income statement or disclose in the notes the portion of the amount recorded in current-period earnings by line item that would have been recorded in previous reporting periods if the adjustment to the provisional amounts had been recognized as of the acquisition date. This ASU is effective for fiscal years, and interim periods within those years, beginning after December 15, 2015. Upon adoption of this ASU in the first quarter of 2016, the Company will apply the guidance in this ASU to future measurement adjustments related to business combinations, as applicable.

In November 2015, the FASB issued ASU 2015-17, Income Taxes (Topic 740): Balance Sheet Classification of Deferred Taxes. The amendments in this ASU require that all deferred tax assets and liabilities be classified as noncurrent on the balance sheet. This ASU is effective for fiscal years, and interim periods within those years, beginning after December 15, 2016. Upon adoption of this ASU in the first quarter of 2017, the current portions of the Company's deferred income tax assets and liabilities will be reclassified as noncurrent assets and liabilities on the consolidated Balance Sheets.

In January 2016, the FASB issued ASU 2016-01, Financial Instruments – Overall (Subtopic 825-10): Recognition and Measurement of Financial Assets and Financial Liabilities. This ASU requires equity investments to be measured at fair value with changes in fair value recognized in net income, and requires enhanced disclosures and presentation of financial assets and liabilities in the financial statements. This ASU also simplifies the impairment assessment of equity investments without readily determinable fair values by requiring a qualitative assessment to identify impairment. This ASU is effective for fiscal years, and interim periods within those years, beginning after December 15, 2017. The Company is currently assessing the impact of adoption of this ASU on its consolidated financial statements.

4. Business Combinations

Acquisition of Woodstock Hydro

On October 31, 2015, Hydro One acquired 100% of the common shares of Woodstock Hydro, an electricity distribution company located in southwestern Ontario. The total purchase price for Woodstock Hydro was approximately $32 million.

The following table summarizes the preliminary determination of the fair value of the assets acquired and liabilities assumed:

(millions of Canadian dollars)	
Cash and cash equivalents	3
Working capital	4
Property, plant and equipment	28
Intangible assets	1
Deferred income tax assets	2
Goodwill	17
long-term debt	(17)
Other long-term liabilities	(2)
Post-retirement and post-employment benefit liability	(1)
Derivative instruments	(3)
	32

The preliminary determination of the fair value of assets acquired and liabilities assumed has been based upon management's preliminary estimates and certain assumptions with respect to the fair values of the assets acquired and liabilities assumed. Due to the timing of the transaction, the Company has not yet completed the final fair value measurements as at December 31, 2015. In addition, the purchase agreement provides for final purchase price adjustments based on agreed working capital and other balances at the acquisition date which have not yet been finalized. The Company will continue to review information and perform further analysis prior to finalizing the total purchase price and the fair values of the assets acquired and liabilities assumed. The actual total purchase price and the fair values of the assets acquired and liabilities assumed may differ from the amounts above.

Goodwill of approximately $17 million arising from the Woodstock Hydro acquisition consists largely of the synergies and economies of scale expected from combining the operations of Hydro One and Woodstock Hydro. All of the goodwill was assigned to Hydro One's Distribution Business segment. Woodstock Hydro contributed revenues of $12 million and net income of $2 million to the Company's consolidated financial results for the year ended December 31, 2015. All costs related to the acquisition have been expensed through the Consolidated Statements of Operations and Comprehensive Income. Woodstock Hydro's financial information is not material to the Company's consolidated financial results for the year ended December 31, 2015 and therefore, has not been disclosed on a pro forma basis.

Hydro One Brampton Spin-off

On August 31, 2015, Hydro One completed the spin-off of its subsidiary, Hydro One Brampton. The spin-off was accounted as a non-monetary, non-reciprocal transfer with the Province, based on its carrying values at August 31, 2015. Transactions that immediately preceded the spin-off as well as the spin-off were as follows:

- Hydro One subscribed for 357 common shares of Hydro One Brampton for an aggregate subscription price of $53 million;
- Hydro One transferred to a company wholly owned by the Province all the issued and outstanding shares of Hydro One Brampton as a dividend in-kind; and all of the long-term intercompany debt in aggregate principal amount of $193 million plus accrued interest of $3 million owed by Hydro One Brampton to Hydro One as a return of stated capital of $196 million on its common shares.

In connection with the Hydro One Brampton spin-off, the following assets and liabilities of Hydro One Brampton were transferred:

(millions of Canadian dollars)	
Working capital	33
Property, plant and equipment and intangibles (net)	360
Other long-term assets	6
long-term liabilities	(205)

As a result of the spin-off, goodwill related to Hydro One Brampton of $60 million was eliminated from the Consolidated Balance Sheet.

Acquisition of Haldimand Hydro

On June 30, 2015, Hydro One acquired 100% of the common shares of Haldimand Hydro, an electricity distribution company located in southwestern Ontario. The final total purchase price for Haldimand Hydro was approximately $73 million.

The following table summarizes the determination of the fair value of the assets acquired and liabilities assumed:

(millions of Canadian dollars)	
Cash and cash equivalents	3
Working capital	5
Property, plant and equipment	52
Deferred income tax assets	1
Goodwill	33
long-term debt	(18)
Regulatory liabilities	(3)
	73

The determination of the fair value of assets acquired and liabilities assumed has been based upon management's estimates and certain assumptions with respect to the fair values of the assets acquired and liabilities assumed.

Goodwill of approximately $33 million arising from the Haldimand Hydro acquisition consists largely of the synergies and economies of scale expected from combining the operations of Hydro One and Haldimand Hydro. All of the goodwill was assigned to Hydro One's Distribution Business segment. Haldimand Hydro contributed revenues of $32 million and net income of $6 million to the Company's consolidated financial results for the year ended December 31, 2015. All costs related to the acquisition have been expensed through the Consolidated Statements of Operations and Comprehensive Income. Haldimand Hydro's financial information is not material to the Company's consolidated financial results for the year ended December 31, 2015 and therefore, has not been disclosed on a pro forma basis.

Acquisition of Norfolk Power

On August 29, 2014, Hydro One acquired 100% of the common shares of Norfolk Power an electricity distribution and telecom company located in southwestern Ontario. Norfolk Power was a holding company for two subsidiaries, Norfolk Power Distribution Inc. (NPDI) and Norfolk Energy Inc.. The total purchase price for Norfolk Power, net of the long-term debt assumed, was approximately $68 million. The purchase price was finalized in 2015, with no adjustments to the preliminary purchase price allocation as disclosed at December 31, 2014.

The following table summarizes the determination of the fair value of the assets acquired and liabilities assumed:

(millions of Canadian dollars)	
Working capital	6
Property, plant and equipment	56
Deferred income tax assets	1
Goodwill	40
Bank indebtedness	(3)
Derivative instruments	(3)
long-term debt	(26)
Post-retirement and post-employment benefit liability	(1)
Environmental liability	(1)
long-term accounts payable and other liabilities	(1)
	68

The determination of the fair values of assets acquired and liabilities assumed has been based upon management's estimates and certain assumptions with respect to the fair values of the assets acquired and liabilities assumed.

Goodwill of approximately $40 million arising from the Norfolk Power acquisition consists largely of the synergies and economies of scale expected from combining the operations of Hydro One and Norfolk Power. All of the goodwill was assigned to Hydro One's Distribution Business segment. Norfolk Power contributed revenues of $18 million and net income of less than $1 million to the Company's consolidated financial results for the year ended December 31, 2014. All costs related to the acquisition have been expensed through the Consolidated Statements of Operations and Comprehensive Income. Norfolk Power's financial information was not material to the Company's consolidated financial results for the year ended December 31, 2014 and therefore, has not been disclosed on a pro forma basis.

5. Depreciation And Amortization

Year ended December 31 *(millions of Canadian dollars)*	2015	2014
Depreciation of property, plant and equipment	595	565
Amortization of intangible assets	54	53
Asset removal costs	91	81
Amortization of regulatory assets	19	23
	759	722

6. Financing Charges

Year ended December 31 *(millions of Canadian dollars)*	2015	2014
Interest on long-term debt	417	432
Other	16	12
less: Interest capitalized on construction and development in progress	(52)	(49)
Gain on interest rate swap agreements	(2)	(10)
Interest earned on investments	(3)	(6)
	376	379

7. Income Taxes

Income taxes / provision for PILs differs from the amount that would have been recorded using the combined Canadian federal and Ontario statutory income tax rate. The reconciliation between the statutory and the effective tax rates is provided as follows:

Year ended December 31 *(millions of Canadian dollars)*	2015	2014
Income taxes / provision for PILs at statutory rate	217	222
Increase (decrease) resulting from:		
Net temporary differences included in amounts charged to customers:		
Capital cost allowance in excess of depreciation and amortization	(37)	(72)
Pension contributions in excess of pension expense	(25)	(24)
Overheads capitalized for accounting but deducted for tax purposes	(15)	(15)
Interest capitalized for accounting but deducted for tax purposes	(13)	(13)
Environmental expenditures	(5)	(5)
Non-refundable investment tax credits	(2)	(3)
Post-retirement and post-employment benefit expense in excess of cash payments	(1)	3
Prior year's adjustments	(1)	(4)
Other	(2)	(1)
Net temporary differences	(101)	(134)
Net tax benefit resulting from transition from PILs Regime to Federal Tax Regime	(19)	–
Hydro One Brampton spin-off	7	–
Net permanent differences	1	1
Total income taxes / provision for PILs	105	89

The major components of income tax expense are as follows:

Year ended December 31 *(millions of Canadian dollars)*	2015	2014
Current income taxes / provision for PILs	2,949	79
Deferred income taxes / provision for (recovery of) PILs	(2,844)	10
Total income taxes / provision for PILs	105	89
Effective income tax rate	12.84%	10.63%

The provision for PILs / current income taxes is remitted to, or received from, the OEFC (PILs Regime) and the CRA (Federal Tax Regime). At December 31, 2015, $12 million (2014 – $39 million) due from the OEFC was included in due from related parties and $1 million (2014 – $nil) due from the CRA was included in prepaid expenses and other assets on the Consolidated Balance Sheet.

In connection with the IPO, Hydro One's exemption from tax under the Federal Tax Regime ceased to apply. Under the PILs Regime, Hydro One was deemed to have disposed of its assets immediately before it lost its tax exempt status under the Federal Tax Regime, resulting in Hydro One making payments in lieu of tax (Departure Tax) totalling $2.6 billion. To enable Hydro One to make the Departure Tax payment, the Province subscribed for common shares of Hydro One for $2.6 billion (See Note 18 – Share Capital). Hydro One used the proceeds of this share subscription to pay the Departure Tax.

At December 31, 2015, the total income taxes / provision for PILs includes deferred income taxes / recovery of PILs of $2,844 million (2014 – deferred provision of $10 million), including $2,810 million (2014 – $nil) resulting from transition from the PILs Regime to the Federal Tax Regime, that is not included in the rate-setting process, using the liability method of accounting. Deferred income taxes / PILs balances expected to be included in the rate-setting process are offset by regulatory assets and liabilities to reflect the anticipated recovery or disposition of these balances within future electricity rates.

Deferred Income Tax Assets and Liabilities

Deferred income tax assets and liabilities arise from differences between the carrying amounts and tax basis of the Company's assets and liabilities. At December 31, 2015 and 2014, deferred income tax assets and liabilities consisted of the following:

December 31 (millions of Canadian dollars)	2015	2014
Deferred income tax assets		
Depreciation and amortization in excess of capital cost allowance	937	(4)
Post-retirement and post-employment benefits expense in excess of cash payments	578	8
Environmental expenditures	75	4
Non-capital losses	62	–
Other	3	(1)
Total deferred income tax assets	1,655	7
less: current portion	19	–
	1,636	7

December 31 (millions of Canadian dollars)	2015	2014
Deferred income tax liabilities		
Regulatory amounts that are not recognized for tax purposes	(153)	(140)
Partnership interest	(41)	(38)
Goodwill	(10)	(21)
Capital cost allowance in excess of depreciation and amortization	(1)	(1,713)
Post-retirement and post-employment benefits expense in excess of cash payments	–	559
Environmental expenditures	–	59
Other	(2)	–
Total deferred income tax liabilities	(207)	(1,294)
less: current portion	–	19
	(207)	(1,313)

During 2015 and 2014, there were no changes in the rate applicable to future taxes. The Company has recorded a valuation allowance in the amount of $278 million (2014 – $nil) in respect of non-depreciable capital property.

8. Accounts Receivable

December 31 (millions of Canadian dollars)	2015	2014
Accounts receivable – billed	379	496
Accounts receivable – unbilled	458	586
Accounts receivable, gross	837	1,082
Allowance for doubtful accounts	(61)	(66)
Accounts receivable, net	776	1,016

In 2015, the Company revised the method to estimate the unbilled accounts receivable by using new technology that improved the estimation process. This change has been accounted for on a prospective basis in the consolidated financial statements at December 31, 2015. At December 31, 2015, the change in estimation technology resulted in a reduction in unbilled accounts receivable of approximately $121 million, with a corresponding offset to various components of the retail settlement variance accounts (RSVA). The change in estimate had no significant impact on 2015 net income.

The following table shows the movements in the allowance for doubtful accounts for the years ended December 31, 2015 and 2014:

Year ended December 31 (millions of Canadian dollars)	2015	2014
Allowance for doubtful accounts – January 1	(66)	(36)
Write-offs	37	24
Additions to allowance for doubtful accounts	(32)	(54)
Allowance for doubtful accounts – December 31	(61)	(66)

9. Property, Plant And Equipment

December 31, 2015 (millions of Canadian dollars)	Property, Plant and Equipment	Accumulated Depreciation	Construction in Progress	Total
Transmission	13,803	4,625	853	10,031
Distribution	9,205	3,177	238	6,266
Communication	1,165	704	28	489
Administration and service	1,531	848	36	719
Easements	523	60	–	463
	26,227	9,414	1,155	17,968

December 31, 2014 (millions of Canadian dollars)	Property, Plant and Equipment	Accumulated Depreciation	Construction in Progress	Total
Transmission	13,209	4,416	626	9,419
Distribution	9,076	3,225	320	6,171
Communication	1,100	615	56	541
Administration and service	1,502	793	23	732
Easements	623	85	–	538
	25,510	9,134	1,025	17,401

Financing charges capitalized on property, plant and equipment under construction were $50 million in 2015 (2014 – $48 million).

10. Intangible Assets

December 31, 2015 (millions of Canadian dollars)	Intangible Assets	Accumulated Amortization	Development in Progress	Total
Computer applications software	579	270	24	333
Other	7	4	–	3
	586	274	24	336

December 31, 2014 (millions of Canadian dollars)	Intangible Assets	Accumulated Amortization	Development in Progress	Total
Computer applications software	573	303	3	273
Other	5	2	–	3
	578	305	3	276

Financing charges capitalized to intangible assets under development were $1 million in 2015 (2014 – $1 million). The estimated annual amortization expense for intangible assets is as follows: 2016 – $57 million; 2017 – $57 million; 2018 – $57 million; 2019 – $47 million; and 2020 – $30 million.

11. Regulatory Assets And Liabilities

Regulatory assets and liabilities arise as a result of the rate-setting process. Hydro One has recorded the following regulatory assets and liabilities:

December 31 *(millions of Canadian dollars)*	2015	2014
Regulatory assets:		
Deferred income tax regulatory asset	1,445	1,327
Pension benefit regulatory asset	952	1,236
Post-retirement and post-employment benefits	240	273
Environmental	207	239
RSVA	110	11
Pension cost variance	37	90
2015-2017 rate rider	20	–
DSC exemption	10	16
Share-based compensation	10	–
B2M LP start-up costs	8	–
OEB cost assessment differential	–	12
Other	12	27
Total regulatory assets	3,051	3,231
Less: current portion	36	31
	3,015	3,200
Regulatory liabilities:		
External revenue variance	87	54
Green Energy expenditure variance	76	83
CDM deferral variance	53	25
Deferred income tax regulatory liability	23	21
PST savings deferral	4	19
Other	12	13
Total regulatory liabilities	255	215
Less: current portion	19	47
	236	168

Deferred Income Tax Regulatory Asset and Liability

Deferred income taxes are recognized on temporary differences between the carrying amount of assets and liabilities in the financial statements and the corresponding tax bases used in the computation of taxable income. The Company has recognized regulatory assets and liabilities that correspond to deferred income taxes that flow through the rate-setting process. In the absence of rate-regulated accounting, the Company's income tax expense would have been recognized using the liability method and there would be no regulatory accounts established for taxes to be recovered through future rates. As a result, the 2015 income tax expense would have been higher by approximately $101 million (2014 – $132 million).

Pension Benefit Regulatory Asset

In accordance with OEB rate orders, pension costs are recorded on a cash basis as employer contributions are paid to the pension fund in accordance with the *Pension Benefits Act* (Ontario). The Company recognizes the net unfunded status of pension obligations on the Consolidated Balance Sheets with an offset to the associated regulatory asset. A regulatory asset is recognized because management considers it to be probable that pension benefit costs will be recovered in the future through the rate-setting process. The pension benefit obligation is remeasured to its fair value at each year end based on an annual actuarial report, with an offset to the associated regulatory asset, to the extent of the remeasurement adjustment. In the absence of rate-regulated accounting, 2015 OCI would have been higher by $284 million (2014 – lower by $391 million).

Post-Retirement and Post-Employment Benefits

The Company recognizes the net unfunded status of post-retirement and post-employment obligations on the Consolidated Balance Sheets with an incremental offset to the associated regulatory assets. A regulatory asset is recognized because management considers it to be probable that post-retirement and post-employment benefit costs will be recovered in the future through the rate-setting process. The post-retirement and post-employment benefit obligation is remeasured to its fair value at each year end based on an annual actuarial report, with an offset to the associated regulatory asset, to the extent of the remeasurement adjustment. In the absence of rate-regulated accounting, 2015 OCI would have been higher by $33 million (2014 – $35 million).

Environmental

Hydro One records a liability for the estimated future expenditures required to remediate environmental contamination. Because such expenditures are expected to be recoverable in future rates, the Company has recorded an equivalent amount as a regulatory asset. In 2015, the environmental regulatory asset decreased by $24 million (2014 – $33 million) to reflect related changes in the Company's PCB liability, and increased by $1 million (2014 – $13 million) due to changes in the land assessment and remediation liability. The environmental regulatory asset is amortized to results of operations based on the pattern of actual expenditures incurred and charged to environmental liabilities. The OEB has the discretion to examine and assess the prudency and the timing of recovery of all of Hydro One's actual environmental expenditures. In the absence of rate-regulated accounting, 2015 operation, maintenance and administration expenses would have been lower by $23 million (2014 – $20 million). In addition, 2015 amortization expense would have been lower by $19 million (2014 – $18 million), and 2015 financing charges would have been higher by $10 million (2014 – $11 million).

RSVA

Hydro One has deferred certain retail settlement variance amounts under the provisions of Article 490 of the OEB's Accounting Procedures Handbook. In March 2015, the OEB approved the disposition of the total RSVA balance accumulated from January 2012 to December 2013, including accrued interest, to be recovered through the 2015-2017 Rate Rider. In 2015, the Company revised its method to estimate the unbilled accounts receivable based on new technology implemented to improve the accuracy of the estimation process. At December 31, 2015, the change in estimate reduced unbilled accounts receivable by approximately $121 million, with a corresponding offset to various components of RSVA. The change in estimate had no significant impact on 2015 net income.

Pension Cost Variance

A pension cost variance account was established for Hydro One Networks' transmission and distribution businesses to track the difference between the actual pension expenses incurred and estimated pension costs approved by the OEB. The balance in this regulatory account reflects the excess of pension costs paid as compared to OEB-approved amounts. In March 2015, the OEB approved the disposition of the distribution business portion of the total pension cost variance account at December 31, 2013, including accrued interest, which will be recovered through the 2015-2017 Rate Rider. In the absence of rate-regulated accounting, 2015 revenue would have been lower by $6 million (2014 – $10 million).

2015-2017 Rate Rider

In March 2015, as part of its decision on Hydro One Networks' Distribution rate application for 2015-2019 the OEB approved the disposition of certain deferral and variance accounts, including RSVAs and accrued interest. The 2015-2017 Rate Rider account includes the balances approved for disposition by the OEB and will be disposed over a 32-month period in accordance with the OEB decision.

DSC Exemption

In June 2010, Hydro One Networks filed an application with the OEB regarding the OEB's new cost responsibility rules contained in the OEB's October 2009 Notice of Amendment to the Distribution System Code (DSC), with respect to the connection of certain renewable generators that were already connected or that had received a connection impact assessment prior to October 21, 2009. The application sought approval to record and defer the unanticipated costs incurred by Hydro One Networks that resulted from the connection of certain renewable generation facilities. The OEB ruled that identified specific expenditures can be recorded in a deferral account subject to the OEB's review in subsequent Hydro One Network distribution applications. In March 2015, the OEB approved the disposition of the DSC exemption deferral account at December 31, 2013, including accrued interest, which will be recovered through the 2015-2017 Rate Rider. In addition, the OEB also approved Hydro One's request to discontinue this deferral account, and there were no additions to this regulatory account in 2015.

Share-based Compensation

The Company recognizes costs associated with stock-based compensation in a regulatory asset as management considers it probable that stock-based compensation costs will be recovered in the future through the rate-setting process. At December 31, 2015 the

stock-based compensation costs relate to the share grant plans, are measured at fair value estimated based on grant date share price and recognized using the graded-vesting attribution method. In the absence of rate-regulated accounting 2015 operation, maintenance and administration expenses would have been higher by $5 million (2014 – $nil).

B2M LP Start-up Costs

In December 2015, OEB issued its decision on B2M LP's application for 2015-2019 and as part of the decision approved the recovery of $8 million of start-up costs relating to B2M LP. The costs will be recovered over a 4 year period beginning in 2016, in accordance with the OEB decision.

OEB Cost Assessment Differential

In April 2010, the OEB issued its Decision regarding Hydro One Networks' distribution rate application for 2010 and 2011. As part of this decision, the OEB also approved the distribution-related OEB Cost Assessment Differential Account to record the difference between the amounts approved in rates and actual expenditures with respect to the OEB's cost assessments. In March 2015, the OEB approved the disposition of the OEB Cost Assessment Differential Account at December 31, 2013, including accrued interest, which will be recovered through the 2015-2017 Rate Rider. In addition, the OEB also approved Hydro One's request to discontinue this deferral account, and there were no additions to this regulatory account in 2015.

External Revenue Variance

In May 2009, the OEB approved forecasted amounts related to export service revenue, external revenue from secondary land use, and external revenue from station maintenance and engineering and construction work. In November 2012, the OEB again approved forecasted amounts related to these revenue categories and extended the scope to encompass all other external revenues. The external revenue variance account balance reflects the excess of actual external revenues compared to the OEB-approved forecasted amounts.

Green Energy Expenditure Variance

In April 2010, the OEB requested the establishment of deferral accounts which capture the difference between the revenue recorded on the basis of Green Energy Plan expenditures incurred and the actual recoveries received.

CDM Deferral Variance Account

As part of Hydro One Networks' application for 2013 and 2014 transmission rates, Hydro One agreed to establish a new regulatory deferral variance account to track the impact of actual Conservation and Demand Management (CDM) and demand response results on the load forecast compared to the estimated load forecast included in the revenue requirement. At December 31, 2014, the balance in the CDM deferral variance account relates to the actual 2013 CDM compared to the amounts included in 2013 revenue requirement. At December 31, 2015, the balance also includes the difference between the actual 2014 CDM compared to the amounts included in 2014 revenue requirement. The OEB rate order specifically states that the IESO (Ontario Power Authority (OPA) prior to January 1, 2015) data used to calculate the difference between forecasted and actual savings will be provided one year in arrears, and as a result, no amount should be recorded in advance of notification from the IESO of actual results.

PST Savings Deferral Account

The provincial sales tax (PST) and goods and services tax (GST) were harmonized in July 2010. Unlike the GST, the PST was included in operation, maintenance and administration expenses or capital expenditures for past revenue requirements approved during a full cost-of-service hearing. Under the harmonized sales tax (HST) regime, the HST included in operation, maintenance and administration expenses or capital expenditures is not a cost ultimately borne by the Company and as such, a refund of the prior PST element in the approved revenue requirement is applicable, and calculations for tracking and refund were requested by the OEB. For Hydro One Networks' transmission revenue requirement, PST was included between July 1, 2010 and December 31, 2010 and recorded in a deferral account, per direction from the OEB. For Hydro One Networks' distribution revenue requirement, PST was included between July 1, 2010 and December 31, 2015 and recorded in a deferral account, as directed by the OEB. In March 2015, the OEB approved the disposition of the PST Savings Deferral account at December 31, 2013, including accrued interest, which will be recovered through the 2015-2017 Rate Rider.

12. Debt And Credit Agreements

Short-Term Notes and Credit Facilities

Hydro One meets its short-term liquidity requirements in part through the issuance of commercial paper under Hydro One Inc.'s Commercial Paper Program which has a maximum authorized amount of $1.5 billion. These short-term notes are denominated in Canadian dollars with varying maturities not exceeding 365 days. The Commercial Paper Program is supported by Hydro One Inc.'s committed revolving credit facilities totalling $2.3 billion. At December 31, 2015, Hydro One Inc. had $1,491 million in commercial paper borrowings outstanding (December 31, 2014 – $nil).

At December 31, 2015, Hydro One's consolidated committed, unsecured and unused credit facilities totalling $2,550 million consisted of the following:

(millions of Canadian dollars)	Maturity	Amount
Hydro One Inc.		
Revolving standby credit facility	June 2020	1,500
Three-year senior, revolving term credit facility	October 2018	800
Hydro One		
Five-year senior, revolving term credit facility	November 2020	250
Total		2,550

The Company may use the credit facilities for working capital and general corporate purposes. If used, interest on the credit facilities would apply based on Canadian benchmark rates. The obligation of each lender to make any credit extension under its credit facility is subject to various conditions including, among other things, that no event of default has occurred or would result from such credit extension.

Long-Term Debt

At December 31, 2015, all of the Company's long-term debt was issued by Hydro One Inc. under Hydro One Inc.'s Medium-Term Note (MTN) Program. The maximum authorized principal amount of notes issuable by Hydro One Inc. under this program is $3.5 billion. At December 31, 2015, $3.5 billion remained available for issuance until January 2018.

The following table presents Hydro One Inc.'s outstanding long-term debt at December 31, 2015 and 2014:

December 31 (millions of Canadian dollars)	2015	2014
2.95% Series 21 notes due 2015[1]	–	500
Floating-rate Series 22 notes due 2015[2]	–	50
4.64% Series 10 notes due 2016	450	450
Floating-rate Series 27 notes due 2016[2]	50	50
5.18% Series 13 notes due 2017	600	600
2.78% Series 28 notes due 2018	750	750
Floating-rate Series 31 notes due 2019[2]	228	228
4.40% Series 20 notes due 2020	300	300
1.62% Series 33 notes due 2020[1]	350	–
3.20% Series 25 notes due 2022	600	600
7.35% Debentures due 2030	400	400
6.93% Series 2 notes due 2032	500	500
6.35% Series 4 notes due 2034	385	385
5.36% Series 9 notes due 2036	600	600
4.89% Series 12 notes due 2037	400	400
6.03% Series 17 notes due 2039	300	300
5.49% Series 18 notes due 2040	500	500
4.39% Series 23 notes due 2041	300	300
6.59% Series 5 notes due 2043	315	315
4.59% Series 29 notes due 2043	435	435
4.17% Series 32 notes due 2044	350	350
5.00% Series 11 notes due 2046	325	325
4.00% Series 24 notes due 2051	225	225
3.79% Series 26 notes due 2062	310	310
4.29% Series 30 notes due 2064	50	50
	8,723	8,923
Add: Unrealized mark-to-market loss[1]	1	2
Less: long-term debt payable within one year	(500)	(552)
long-term debt	8,224	8,373

[1] The unrealized mark-to-market loss relates to $50 million of the Series 33 notes due 2020 (2014 – $250 million of the Series 21 notes due 2015). The unrealized mark-to-market loss is offset by a $1 million (2014 – $2 million) unrealized mark-to-market gain on the related fixed-to-floating interest-rate swap agreements, which are accounted for as fair value hedges. See Note 13 – Fair Value of Financial Instruments and Risk Management for details of fair value hedges.

[2] The interest rates of the floating-rate notes are referenced to the 3-month Canadian dollar bankers' acceptance rate, plus a margin.

In 2015, Hydro One Inc. issued $350 million (2014 – $628 million) of long-term debt under the MTN Program, and repaid $550 million of long-term debt MTN Program notes (2014 – $750 million).

Long-term debt totalling $35 million assumed by Hydro One Inc. as part of the Haldimand Hydro and Woodstock Hydro acquisitions was repaid in 2015.

The long-term debt is unsecured and denominated in Canadian dollars. The long-term debt is summarized by the number of years to maturity in Note 13 – Fair Value of Financial Instruments and Risk Management.

13. Fair Value of Financial Instruments and Risk Management

Fair value is considered to be the exchange price in an orderly transaction between market participants to sell an asset or transfer a liability at the measurement date. The fair value definition focuses on an exit price, which is the price that would be received in the sale of an asset or the amount that would be paid to transfer a liability.

Hydro One classifies its fair value measurements based on the following hierarchy, as prescribed by the accounting guidance for

fair value, which prioritizes the inputs to valuation techniques used to measure fair value into three levels:

level 1 inputs are unadjusted quoted prices in active markets for identical assets or liabilities that Hydro One has the ability to access. An active market for the asset or liability is one in which transactions for the asset or liability occur with sufficient frequency and volume to provide ongoing pricing information.

level 2 inputs are those other than quoted market prices that are observable, either directly or indirectly, for an asset or liability. level 2 inputs include, but are not limited to, quoted prices for similar assets or liabilities in an active market, quoted prices for identical or similar assets or liabilities in markets that are not active and inputs other than quoted market prices that are observable for the asset or liability, such as interest rate curves and yield curves observable at commonly quoted intervals, volatilities, credit risk and default rates. A level 2 measurement cannot have more than an insignificant portion of the valuation based on unobservable inputs.

level 3 inputs are any fair value measurements that include unobservable inputs for the asset or liability for more than an insignificant portion of the valuation. A level 3 measurement may be based primarily on level 2 inputs.

Non-Derivative Financial Assets and Liabilities

At December 31, 2015 and 2014, the Company's carrying amounts of accounts receivable, due from related parties, cash and cash equivalents, bank indebtedness, short-term notes payable, accounts payable, and due to related parties are representative of fair value because of the short-term nature of these instruments.

Fair Value Measurements of Long-Term Debt

The fair values and carrying values of the Company's long-term debt at December 31, 2015 and 2014 are as follows:

December 31 *(millions of Canadian dollars)*	2015 Carrying Value	2015 Fair Value	2014 Carrying Value	2014 Fair Value
long-term debt				
$250 million of MTN Series 21 notes[1]	–	–	252	252
$50 million of MTN Series 33 notes[1]	51	51	–	–
Other notes and debentures[2]	8,673	9,942	8,673	10,159
	8,724	9,993	8,925	10,411

[1] The fair value of the $50 million MTN Series 33 notes and $250 million of the MTN Series 21 notes subject to hedging is primarily based on changes in the present value of future cash flows due to a change in the yield in the swap market for the related swap (hedged risk).

[2] The fair value of other notes and debentures, and the portion of the MTN Series 21 notes that are not subject to hedging, represents the market value of the notes and debentures and is based on unadjusted period-end market prices for the same or similar debt of the same remaining maturities.

Fair Value Measurements of Derivative Instruments

At December 31, 2015, Hydro One Inc. had an interest rate swap in the amount of $50 million (2014 – $250 million) that was used to convert fixed rate debt to floating rate debt. This swap is classified as a fair value hedge. Hydro One Inc.'s fair value hedge exposure was equal to about 1% (2014 – 3%) of its total long-term debt of $8,724 million (2014 – $8,925 million). At December 31, 2015, Hydro One Inc.'s interest rate swap designated as a fair value hedge was as follows:

- a $50 million fixed to floating interest rate swap agreement to convert $50 million of the $350 million MTN Series 33 notes maturing April 30, 2020 into three-month variable rate debt.

At December 31, 2015, the Company had no interest rate swaps classified as undesignated contracts (2014 – $409 million).

As part of the Norfolk Power and Woodstock Hydro acquisitions, Hydro One Inc. assumed liabilities associated with unrealized losses on derivative instruments (interest rate swaps) totalling $6 million. Hydro One Inc. extinguished the interest rate swaps and repaid these liabilities in 2015.

Fair Value Hierarchy

The fair value hierarchy of financial assets and liabilities at December 31, 2015 and 2014 is as follows:

December 31, 2015 *(millions of Canadian dollars)*	Carrying Value	Fair Value	Level 1	Level 2	Level 3
Assets:					
Cash and cash equivalents	94	94	94	–	–
Derivative instruments					
Fair value hedge – interest-rate swap	1	1	1	–	–
	95	95	95	–	–
Liabilities:					
Short-term notes payable	1,491	1,491	1,491	–	–
Long-term debt	8,724	9,993	–	9,993	–
	10,215	11,484	1,491	9,993	–

December 31, 2014 *(millions of Canadian dollars)*	Carrying Value	Fair Value	Level 1	Level 2	Level 3
Assets:					
Cash and cash equivalents	100	100	100	–	–
Derivative instruments					
Fair value hedges – interest-rate swaps	2	2	–	2	–
	102	102	100	2	–
Liabilities:					
Bank indebtedness	2	2	2	–	–
Derivative instruments					
Undesignated contracts – interest-rate swaps	3	3	–	3	–
Long-term debt	8,925	10,411	–	10,411	–
	8,930	10,416	2	10,414	–

Cash and cash equivalents include cash and short-term investments. The carrying values are representative of fair value because of the short-term nature of these instruments.

The fair value of the derivative instruments is determined using inputs other than quoted prices that are observable for these assets. The fair value is primarily based on the present value of future cash flows using a swap yield curve to determine the assumptions for interest rates.

The fair value of the hedged portion of the long-term debt is primarily based on the present value of future cash flows using a swap yield curve to determine the assumption for interest rates. The fair value of the unhedged portion of the long-term debt is based on unadjusted period-end market prices for the same or similar debt of the same remaining maturities.

There were no significant transfers between any of the fair value levels during the years ended December 31, 2015 and 2014.

Risk Management

Exposure to market risk, credit risk and liquidity risk arises in the normal course of the Company's business.

Market Risk

Market risk refers primarily to the risk of loss that results from changes in costs, foreign exchange rates and interest rates. The Company is exposed to fluctuations in interest rates as its regulated return on equity is derived using a formulaic approach that takes into account anticipated interest rates, but is not currently exposed to material commodity price risk or material foreign exchange risk.

The OEB-approved adjustment formula for calculating return on equity in a deemed regulatory capital structure of 60% debt and 40% equity provides for increases and decreases depending on changes in benchmark rates of return for Government of Canada debt. The Company estimates that a 1% decrease in the forecasted long-term Government of Canada bond yield used in determining its rate of return would reduce the Company's transmission business' 2015 net income by approximately $20 million (2014 – $20 million) and its distribution business' 2015 net income by approximately $13 million (2014 – $10 million). The Company's net income is adversely impacted by rising interest rates as the Company's maturing long-term debt is refinanced at market rates. The Company periodically utilizes interest rate swap agreements to mitigate elements of interest rate risk.

The Company uses a combination of fixed and variable-rate debt to manage the mix of its debt portfolio. The Company also uses derivative financial instruments to manage interest-rate risk. The Company utilizes interest-rate swaps, which are typically designated as fair value hedges, as a means to manage its interest rate exposure to achieve a lower cost of debt. In addition, the Company may utilize interest-rate derivative instruments to lock in interest-rate levels in anticipation of future financing.

A hypothetical 10% increase in the interest rates associated with variable-rate debt would not have resulted in a significant decrease in Hydro One's net income for the years ended December 31, 2015 or 2014.

Fair Value Hedges

For derivative instruments that are designated and qualify as fair value hedges, the gain or loss on the derivative as well as the offsetting loss or gain on the hedged item attributable to the hedged risk are recognized in the Consolidated Statements of Operations and Comprehensive Income. The net unrealized loss (gain) on the hedged debt and the related interest-rate swaps for the years ended December 31, 2015 and 2014 are included in financing charges as follows:

Year ended December 31 *(millions of Canadian dollars)*	2015	2014
Unrealized loss (gain) on hedged debt	(1)	(3)
Unrealized loss (gain) on fair value interest-rate swaps	1	3
Net unrealized loss (gain)	–	–

At December 31, 2015, Hydro One had $50 million (2014 – $250 million) of notional amounts of fair value hedges outstanding related to interest-rate swaps, with assets at fair value of $1 million (2014 – $2 million). During the years ended December 31, 2015 and 2014, there was no significant impact on the results of operations as a result of any ineffectiveness attributable to fair value hedges.

Credit Risk

Financial assets create a risk that a counterparty will fail to discharge an obligation, causing a financial loss. At December 31, 2015 and 2014, there were no significant concentrations of credit risk with respect to any class of financial assets. The Company's revenue is earned from a broad base of customers. As a result, Hydro One did not earn a significant amount of revenue from any single customer. At December 31, 2015 and 2014, there was no significant accounts receivable balance due from any single customer.

At December 31, 2015, the Company's provision for bad debts was $61 million (2014 – $66 million). Adjustments and write-offs were determined on the basis of a review of overdue accounts, taking into consideration historical experience. At December 31, 2015, approximately 6% (2014 – 6%) of the Company's net accounts receivable were aged more than 60 days.

Hydro One manages its counterparty credit risk through various techniques including: entering into transactions with highly-rated counterparties; limiting total exposure levels with individual counterparties consistent with the Company's Board-approved Credit Risk Policy; entering into master agreements which enable net settlement and the contractual right of offset; and monitoring the financial condition of counterparties. In addition to payment netting language in master agreements, the Company establishes credit limits, margining thresholds and collateral requirements for each counterparty. Counterparty credit limits are based on an internal credit review that considers a variety of factors, including the results of a scoring model, leverage, liquidity, profitability, credit ratings and risk management capabilities. The determination of credit exposure for a particular counterparty is the sum of current exposure plus the potential future exposure with that counterparty. The current exposure is calculated as the sum of the principal value of money market exposures and the market value of all contracts that have a positive mark-to-market position on the measurement date. The Company would offset the positive market values against negative values with the same counterparty only where permitted by the existence of a legal netting agreement such as an International Swap Dealers Association master agreement. The potential future exposure represents a safety margin to protect against future fluctuations of interest rates, currencies, equities, and commodities. It is calculated

based on factors developed by the Bank of International Settlements, following extensive historical analysis of random fluctuations of interest rates and currencies. To the extent that a counterparty's margining thresholds are exceeded, the counterparty is required to post collateral with the Company as specified in each agreement. The Company monitors current and forward credit exposure to counterparties both on an individual and an aggregate basis. The Company's credit risk for accounts receivable is limited to the carrying amounts on the Consolidated Balance Sheets.

Derivative financial instruments result in exposure to credit risk since there is a risk of counterparty default. The credit exposure of derivative contracts, before collateral, is represented by the fair value of contracts at the reporting date. At December 31, 2015, the counterparty credit risk exposure on the fair value of these interest rate swap contracts was $1 million (2014 – $3 million). At December 31, 2015, Hydro One's credit exposure for all derivative instruments, and applicable payables and receivables, had a credit rating of investment grade, with one financial institution as the counterparty.

Liquidity Risk

Liquidity risk refers to the Company's ability to meet its financial obligations as they come due. Hydro One meets its short-term liquidity requirements using cash and cash equivalents on hand, funds from operations, the issuance of commercial paper, and the revolving standby facilities totaling $2,550 million. The short-term liquidity under the Commercial Paper Program, and anticipated levels of funds from operations should be sufficient to fund normal operating requirements.

At December 31, 2015, accounts payable and accrued liabilities in the amount of $753 million (2014 – $784 million) were expected to be settled in cash at their carrying amounts within the next 12 months.

At December 31, 2015, Hydro One Inc. had long-term debt in the principal amount of $8,723 million (2014 – $8,923 million). Principal repayments and related weighted average interest rates are summarized by the number of years to maturity in the following table:

Years to Maturity	Long-term Debt Principal Repayments *(millions of Canadian dollars)*	Weighted Average Interest Rate *(%)*
1 year	500	4.3
2 years	600	5.2
3 years	750	2.8
4 years	228	1.2
5 years	650	2.9
	2,728	3.5
6 – 10 years	600	3.2
Over 10 years	5,395	5.4
	8,723	4.7

Interest payments on long-term debt are summarized by year in the following table:

Year	Interest Payments *(millions of Canadian dollars)*
2016	397
2017	386
2018	355
2019	332
2020	322
	1,792
2021-2025	1,496
2026 +	4,080
	7,368

14. Capital Management

The Company's objectives with respect to its capital structure are to maintain effective access to capital on a long-term basis at reasonable rates, and to deliver appropriate financial returns. In order to ensure ongoing access to capital, the Company targets to maintain strong credit quality. The Company considers its capital structure to consist of shareholders' equity, including preferred shares, long-term debt, short-term notes payable, and cash and cash equivalents. At December 31, 2015 and 2014, the Company's capital structure was as follows:

December 31 *(millions of Canadian dollars)*	2015	2014
Long-term debt payable within one year	500	552
Short-term notes payable	1,491	–
Less: cash and cash equivalents	94	100
	1,897	452
Long-term debt	8,224	8,373
Preferred shares	418	323
Common shares	5,623	3,314
Retained earnings	3,806	4,249
	9,429	7,563
Total capital	19,968	16,711

Hydro One Inc. has customary covenants typically associated with long-term debt. Among other things, Hydro One Inc.'s long-term debt and credit facility covenants limit the permissible debt to 75% of its total capitalization, limit the ability to sell assets and impose a negative pledge provision, subject to customary exceptions. At December 31, 2015 and 2014, Hydro One Inc. was in compliance with all of these covenants and limitations.

15. Pension and Post-retirement and Post-Employment Benefits

Hydro One has a defined benefit pension plan, a supplementary pension plan, and post-retirement and post-employment benefit plans. The defined benefit pension plan (Pension Plan) is contributory and covers all regular employees of Hydro One and its subsidiaries, except employees of Haldimand Hydro and Woodstock Hydro. Employees of Haldimand Hydro and Woodstock Hydro participate in the OMERS Plan. The supplementary pension plan provides members of the Pension Plan with benefits that would have been earned and payable under the Pension Plan but for limitations imposed by the *Income Tax Act* (Canada). The supplementary pension plan obligation is included with other post-retirement and post-employment benefit obligations on the Consolidated Balance Sheets.

The OMERS Plan

Hydro One contributions to the OMERS Plan for the year ended December 31, 2015 were $2 million (2014 – $2 million). At December 31, 2015, Company contributions payable included in accrued liabilities on the Consolidated Balance Sheets were less than $1 million (2014 – less than $1 million). Hydro One contributions do not represent more than 5% of total contributions to the OMERS Plan, as indicated in OMERS' most recently available annual report for the year ended December 31, 2014.

At December 31, 2014, the OMERS Plan was 90.8% funded, with an unfunded liability of $7.1 billion. This unfunded liability could result in future payments by participating employers and members. Hydro One future contributions could be increased substantially if other entities withdraw from the plan.

Pension Plan, Post-Retirement and Post-Employment Plans

The Pension Plan provides benefits based on highest three-year average pensionable earnings. For new management employees who commenced employment on or after January 1, 2004, and for new Society of Energy Professionals represented staff hired after November 17, 2005, benefits are based on highest five-year average pensionable earnings. After retirement, pensions are indexed to inflation.

Company and employee contributions to the Pension Plan are based on actuarial valuations performed at least every three years. Annual Pension Plan contributions for 2015 of $177 million (2014 – $174 million) were based on an actuarial valuation effective December 31, 2013 and the expected level of pensionable

earnings. Estimated annual Pension Plan contributions for 2016 are approximately $180 million, based on the actuarial valuation as at December 31, 2013 and projected levels of pensionable earnings. Future minimum contributions beyond 2016 will be based on an actuarial valuation effective no later than December 31, 2016. Contributions are payable one month in arrears. All of the contributions are expected to be in the form of cash.

Hydro One recognizes the overfunded or underfunded status of the Pension Plan, and post-retirement and post-employment benefit plans (Plans) as an asset or liability on its Consolidated Balance Sheets, with offsetting regulatory assets and liabilities as appropriate. The underfunded benefit obligations for the Plans, in the absence of regulatory accounting, would be recognized in AOCI. The impact of changes in assumptions used to measure pension, post-retirement and post-employment benefit obligations is generally recognized over the expected average remaining service period of the employees. The measurement date for the Plans is December 31.

Year ended December 31	Pension Benefits		Post Retirement and Post Employment Benefits	
(millions of Canadian dollars)	2015	2014	2015	2014
Change in projected benefit obligation				
Projected benefit obligation, beginning of year	7,535	6,576	1,582	1,531
Current service cost	186	145	43	41
Interest cost	302	312	64	73
Benefits paid	(334)	(319)	(47)	(45)
Net actuarial loss (gain)	(6)	821	(27)	(18)
Change due to Hydro One Brampton spin-off	–	–	(5)	–
Projected benefit obligation, end of year	7,683	7,535	1,610	1,582
Change in plan assets				
Fair value of plan assets, beginning of year	6,299	5,731	–	–
Actual return on plan assets	582	703	–	–
Benefits paid	(334)	(319)	–	–
Employer contributions	177	174	–	–
Employee contributions	40	35	–	–
Administrative expenses	(33)	(25)	–	–
Fair value of plan assets, end of year	6,731	6,299	–	–
Unfunded status	952	1,236	1,610	1,582

Hydro One presents its benefit obligations and plan assets net on its Consolidated Balance Sheets within the following line items:

December 31	Pension Benefits		Post Retirement and Post Employment Benefits	
(millions of Canadian dollars)	2015	2014	2015	2014
Accrued liabilities	–	–	50	49
Pension benefit liability	952	1,236	–	–
Post-retirement and post-employment benefit liability	–	–	1,560	1,533
Unfunded status	952	1,236	1,610	1,582

The funded or unfunded status of the pension, post-retirement and post-employment benefit plans refers to the difference between the fair value of plan assets and the projected benefit obligations for the Plans. The funded/unfunded status changes over time due to several factors, including contribution levels, assumed discount rates and actual returns on plan assets.

The following table provides the projected benefit obligation (PBO), accumulated benefit obligation (ABO) and fair value of plan assets for the Pension Plan:

December 31 *(millions of Canadian dollars)*	2015	2014
PBO	7,683	7,535
ABO	7,020	6,887
Fair value of plan assets	6,731	6,299

On an ABO basis, the Pension Plan was funded at 96% at December 31, 2015 (2014 – 91%). On a PBO basis, the Pension Plan was funded at 88% at December 31, 2015 (2014 – 84%). The ABO differs from the PBO in that the ABO includes no assumption about future compensation levels.

Components of Net Periodic Benefit Costs

The following table provides the components of the net periodic benefit costs for the years ended December 31, 2015 and 2014 for the Pension Plan:

Year ended December 31 *(millions of Canadian dollars)*	2015	2014
Current service cost, net of employee contributions	146	110
Interest cost	302	312
Expected return on plan assets, net of expenses	(406)	(369)
Actuarial loss amortization	119	103
Prior service cost amortization	2	2
Net periodic benefit costs	163	158
Charged to results of operations[1]	81	81

[1] The Company follows the cash basis of accounting consistent with the inclusion of pension costs in OEB-approved rates. During the year ended December 31, 2015, pension costs of $177 million (2014 – $174 million) were attributed to labour, of which $81 million (2014 – $81 million) was charged to operations, and $96 million (2014 – $93 million) was capitalized as part of the cost of property, plant and equipment and intangible assets.

The following table provides the components of the net periodic benefit costs for the years ended December 31, 2015 and 2014 for the post retirement and post-employment benefit plans:

Year ended December 31 *(millions of Canadian dollars)*	2015	2014
Current service cost, net of employee contributions	43	41
Interest cost	64	73
Actuarial loss amortization	14	18
Prior service cost amortization	–	2
Net periodic benefit costs	121	134
Charged to results of operations	55	62

Assumptions

The measurement of the obligations of the Plans and the costs of providing benefits under the Plans involves various factors, including the development of valuation assumptions and accounting policy elections. When developing the required assumptions, the Company considers historical information as well as future expectations. The measurement of benefit obligations and costs is impacted by several assumptions including the discount rate applied to benefit obligations, the long-term expected rate of return on plan assets, Hydro One's expected level of contributions to the Plans, the incidence of mortality, the expected remaining service period of plan participants, the level of compensation and rate of compensation increases, employee age, length of service, and the anticipated rate of increase of health care costs, among other factors. The impact of changes in assumptions

used to measure the obligations of the Plans is generally recognized over the expected average remaining service period of the plan participants. In selecting the expected rate of return on plan assets, Hydro One considers historical economic indicators that impact asset returns, as well as expectations regarding future long-term capital market performance, weighted by target asset class allocations. In general, equity securities, real estate and private equity investments are forecasted to have higher returns than fixed income securities.

The following weighted average assumptions were used to determine the benefit obligations at December 31, 2015 and 2014:

	Pension Benefits		Post-Retirement and Post-Employment Benefits	
Year ended December 31	2015	2014	2015	2014
Significant assumptions:				
Weighted average discount rate	4.00%	4.00%	4.10%	4.00%
Rate of compensation scale escalation (without merit)	2.50%	2.50%	2.50%	2.50%
Rate of cost of living increase	2.00%	2.00%	2.00%	2.00%
Rate of increase in health care cost trends[1]	–	–	4.36%	4.36%

[1] 6.38% per annum in 2016, grading down to 4.36% per annum in and after 2031 (2014 – 6.52% in 2015, grading down to 4.36% per annum in and after 2031)

The following weighted average assumptions were used to determine the net periodic benefit costs for the years ended December 31, 2015 and 2014. Assumptions used to determine current year-end benefit obligations are the assumptions used to estimate the subsequent year's net periodic benefit costs.

Year ended December 31	2015	2014
Pension Benefits:		
Weighted average expected rate of return on plan assets	6.50%	6.50%
Weighted average discount rate	4.00%	4.75%
Rate of compensation scale escalation (without merit)	2.50%	2.50%
Rate of cost of living increase	2.00%	2.00%
Average remaining service life of employees *(years)*	13	11
Post-Retirement and Post-Employment Benefits:		
Weighted average discount rate	4.00%	4.75%
Rate of compensation scale escalation (without merit)	2.50%	2.50%
Rate of cost of living increase	2.00%	2.00%
Average remaining service life of employees *(years)*	13.8	12
Rate of increase in health care cost trends[1]	4.36%	4.39%

[1] 6.52% per annum in 2015, grading down to 4.36% per annum in and after 2031 (2014 – 6.81% in 2014, grading down to 4.39% per annum in and after 2031)

The discount rate used to determine the current year pension obligation and the subsequent year's net periodic benefit costs is based on a yield curve approach. Under the yield curve approach, expected future benefit payments for each plan are discounted by a rate on a third party bond yield curve corresponding to each duration. The yield curve is based on "AA" long-term corporate bonds. A single discount rate is calculated that would yield the same present value as the sum of the discounted cash flows.

The effect of a 1% change in health care cost trends on the projected benefit obligation for the post-retirement and post-employment benefits at December 31, 2015 and 2014 is as follows:

December 31 *(millions of Canadian dollars)*	2015	2014
Projected benefit obligation:		
Effect of a 1% increase in health care cost trends	252	248
Effect of a 1% decrease in health care cost trends	(196)	(193)

The effect of a 1% change in health care cost trends on the service cost and interest cost for the post-retirement and post-employment benefits for the years ended December 31, 2015 and 2014 is as follows:

Year ended December 31 *(millions of Canadian dollars)*	2015	2014
Service cost and interest cost:		
Effect of a 1% increase in health care cost trends	22	23
Effect of a 1% decrease in health care cost trends	(16)	(17)

The following approximate life expectancies were used in the mortality assumptions to determine the projected benefit obligations for the pension and post-retirement and post-employment plans at December 31, 2015 and 2014:

December 31, 2015 Life expectancy at 65 for a member currently at				December 31, 2014 Life expectancy at 65 for a member currently at			
Age 65		Age 45		Age 65		Age 45	
Male	**Female**	**Male**	**Female**	Male	Female	Male	Female
23	**25**	**24**	**26**	23	25	24	26

Estimated Future Benefit Payments

At December 31, 2015, estimated future benefit payments to the participants of the Plans were:

(millions of Canadian dollars)	Pension Benefits	Post-Retirement and Post-Employment Benefits
2016	316	53
2017	328	55
2018	339	57
2019	350	59
2020	360	61
2021 through to 2025	1,928	342
Total estimated future benefit payments through to 2025	3,621	627

Components of Regulatory Assets

A portion of actuarial gains and losses and prior service costs is recorded within regulatory assets on Hydro One's Consolidated Balance Sheets to reflect the expected regulatory inclusion of these amounts in future rates, which would otherwise be recorded in OCI. The following table provides the actuarial gains and losses and prior service costs recorded within regulatory assets:

Year ended December 31 *(millions of Canadian dollars)*	2015	2014
Pension Benefits:		
Actuarial loss (gain) for the year	(181)	511
Actuarial loss amortization	(119)	(103)
Prior service cost amortization	(2)	(2)
	(302)	406
Post-Retirement and Post-Employment Benefits:		
Actuarial loss (gain) for the year	(27)	(18)
Actuarial loss amortization	(14)	(18)
Prior service cost amortization	–	(2)
	(41)	(38)

The following table provides the components of regulatory assets that have not been recognized as components of net periodic benefit costs for the years ended December 31, 2015 and 2014:

Year ended December 31 *(millions of Canadian dollars)*	2015	2014
Pension Benefits:		
Prior service cost	–	2
Actuarial loss	952	1,234
	952	1,236
Post-Retirement and Post-Employment Benefits:		
Actuarial loss	240	273
	240	273

The following table provides the components of regulatory assets at December 31 that are expected to be amortized as components of net periodic benefit costs in the following year:

December 31	Pension Benefits		Post-Retirement and Post-Employment Benefits	
(millions of Canadian dollars)	2015	2014	2015	2014
Prior service cost	–	2	–	–
Actuarial loss	96	119	8	10
	96	121	8	10

Pension Plan Assets

Investment Strategy

On a regular basis, Hydro One evaluates its investment strategy to ensure that Pension Plan assets will be sufficient to pay Pension Plan benefits when due. As part of this ongoing evaluation, Hydro One may make changes to its targeted asset allocation and investment strategy. The Pension Plan is managed at a net asset level. The main objective of the Pension Plan is to sustain a certain level of net assets in order to meet the pension obligations of the Company. The Pension Plan fulfills its primary objective by adhering to specific investment policies outlined in its Summary of Investment Policies and Procedures (SIPP), which is reviewed and approved by the Human Resource Committee of Hydro One's Board of Directors. The Company manages net assets by engaging knowledgeable external investment managers who are charged with the responsibility of investing existing funds and new funds (current year's employee and employer contributions) in accordance with the approved SIPP. The performance of the managers is monitored through a governance structure. Increases in net assets are a direct result of investment income generated by investments held by the Pension Plan and contributions to the Pension Plan by eligible employees and by the Company. The main use of net assets is for benefit payments to eligible Pension Plan members.

Pension Plan Asset Mix

At December 31, 2015, the Pension Plan target asset allocations and weighted average asset allocations were as follows:

	Target Allocation (%)	Pension Plan Assets (%)
Equity securities	55.0	58.2
Debt securities	35.0	36.4
Other[1]	10.0	5.4
	100.0	100.0

[1] Other investments include real estate and infrastructure investments.

At December 31, 2015, the Pension Plan held $9 million Hydro One corporate bonds (2014 – $nil) and $420 million of debt securities of the Province (2014 – $340 million).

Concentrations of Credit Risk

Hydro One evaluated its Pension Plan's asset portfolio for the existence of significant concentrations of credit risk as at December 31, 2015 and 2014. Concentrations that were evaluated include, but are not limited to, investment concentrations in a single entity, concentrations in a type of industry, and concentrations in individual funds. At December 31, 2015 and 2014, there were no significant concentrations (defined as greater than 10% of plan assets) of risk in the Pension Plan's assets.

The Pension Plan manages its counterparty credit risk with respect to bonds by investing in investment grade and government bonds and with respect to derivative instruments by transacting only with financial institutions rated at least "A+" by Standard & Poor's Rating Services, DBRS Limited, and Fitch Ratings Inc., and "A1" by Moody's Investors Service, and also by utilizing exposure limits to each counterparty and ensuring that exposure is diversified across counterparties. The risk of default on transactions in listed securities is considered minimal, as the trade will fail if either party to the transaction does not meet its obligation.

Fair Value Measurements

The following tables present the Pension Plan assets measured and recorded at fair value on a recurring basis and their level within the fair value hierarchy at December 31, 2015 and 2014:

December 31, 2015 (millions of Canadian dollars)	Level 1	Level 2	Level 3	Total
Pooled funds	–	23	299	322
Cash and cash equivalents	191	–	–	191
Short-term securities	–	80	–	80
Real estate	–	–	2	2
Corporate shares – Canadian	923	–	–	923
Corporate shares – Foreign	2,931	–	–	2,931
Bonds and debentures – Canadian	–	2,074	–	2,074
Bonds and debentures – Foreign	–	199	–	199
Total fair value of plan assets[1]	4,045	2,376	301	6,722

[1] At December 31, 2015, the total fair value of Pension Plan assets excludes $27 million of interest and dividends receivable, and $18 million relating to accruals for pension administration expense and foreign exchange contracts payable.

December 31, 2014 (millions of Canadian dollars)	Level 1	Level 2	Level 3	Total
Pooled funds	–	18	142	160
Cash and cash equivalents	166	–	–	166
Short-term securities	–	176	–	176
Real estate	–	–	2	2
Corporate shares – Canadian	1,008	–	–	1,008
Corporate shares – Foreign	2,766	–	–	2,766
Bonds and debentures – Canadian	–	1,799	–	1,799
Bonds and debentures – Foreign	–	211	–	211
Total fair value of plan assets[1]	3,940	2,204	144	6,288

[1] At December 31, 2014, the total fair value of Pension Plan assets excludes $18 million of interest and dividends receivable, and $7 million relating to accruals for pension administration expense.

See Note 13 – Fair Value of Financial Instruments and Risk Management for a description of levels within the fair value hierarchy.

Changes in the Fair Value of Financial Instruments Classified in Level 3

The following table summarizes the changes in fair value of financial instruments classified in Level 3 for the years ended December 31, 2015 and 2014. The Pension Plan classifies financial instruments as Level 3 when the fair value is measured based on at least one significant input that is not observable in the markets or due to lack of liquidity in certain markets. The gains and losses presented in the table below may include changes in fair value based on both observable and unobservable inputs.

Year ended December 31 (millions of Canadian dollars)	2015	2014
Fair value, beginning of year	144	119
Realized and unrealized gains	51	30
Purchases	106	23
Sales and disbursements	–	(28)
Fair value, end of year	301	144

There were no significant transfers between any of the fair value levels during the years ended December 31, 2015 and 2014.

The Company performs sensitivity analysis for fair value measurements classified in Level 3, substituting the unobservable inputs with one or more reasonably possible alternative assumptions. These sensitivity analyses resulted in negligible changes in the fair value of financial instruments classified in this level.

Valuation Techniques Used to Determine Fair Value

Pooled Funds

The pooled fund category mainly consists of private equity, real estate and infrastructure investments. Private equity investments represent private equity funds that invest in operating companies that are not publicly traded on a stock exchange. Investment strategies in private equity include limited partnerships in businesses that are characterized by high internal growth and operational efficiencies, venture capital, leveraged buyouts and special situations such as distressed investments. Real estate and infrastructure investments represent funds that invest in real assets which are not publicly traded on a stock exchange. Investment strategies in real estate include limited partnerships that seek to generate a total return through income and capital growth by investing primarily in global and Canadian limited partnerships. Investment strategies in infrastructure include limited partnerships in core infrastructure assets focusing on assets that generate stable, long-term cash flows and deliver incremental returns relative to conventional fixed income investments. Private equity, real estate and infrastructure valuations are reported by the fund manager and are based on the valuation of the underlying investments which includes inputs such as cost, operating results, discounted future cash flows and market-based comparable data. Since these valuation inputs are not highly observable, private equity and infrastructure investments have been categorized as Level 3 within pooled funds.

Cash Equivalents

Demand cash deposits held with banks and cash held by the investment managers are considered cash equivalents and are included in the fair value measurements hierarchy as Level 1.

Short-Term Securities

Short-term securities are valued at cost plus accrued interest, which approximates fair value due to their short-term nature. Short-term securities have been categorized as Level 2.

Real Estate

Real estate investments represent investments in holding companies that invest in real estate properties. The investments in the holding companies are valued using net asset values reported by the fund manager. Real estate investments are categorized as Level 3.

Corporate Shares

Corporate shares are valued based on quoted prices in active markets and are categorized as Level 1. Investments denominated in foreign currencies are translated into Canadian currency at year-end rates of exchange.

Bonds and Debentures

Bonds and debentures are presented at published closing trade quotations, and are categorized as Level 2.

16. Environmental Liabilities

The following tables show the movements in environmental liabilities for the years ended December 31, 2015 and 2014:

Year ended December 31, 2015 *(millions of Canadian dollars)*	PCB	Land Assessment and Remediation	Total
Environmental liabilities, January 1	172	67	239
Interest accretion	8	2	10
Expenditures	(8)	(11)	(19)
Revaluation adjustment	(24)	1	(23)
Environmental liabilities, December 31	148	59	207
less: current portion	12	10	22
	136	49	185

Year ended December 31, 2014 *(millions of Canadian dollars)*	PCB	Land Assessment and Remediation	Total
Environmental liabilities, January 1	201	65	266
Interest accretion	9	2	11
Expenditures	(5)	(13)	(18)
Revaluation adjustment	(33)	13	(20)
Environmental liabilities, December 31	172	67	239
Less: current portion	8	10	18
	164	57	221

The following tables show the reconciliation between the undiscounted basis of the environmental liabilities and the amount recognized on the Consolidated Balance Sheets after factoring in the discount rate:

December 31, 2015 *(millions of Canadian dollars)*	**PCB**	**Land Assessment and Remediation**	**Total**
Undiscounted environmental liabilities	**168**	**61**	**229**
Less: discounting accumulated liabilities to present value	**20**	**2**	**22**
Discounted environmental liabilities	**148**	**59**	**207**

December 31, 2014 *(millions of Canadian dollars)*	PCB	Land Assessment and Remediation	Total
Undiscounted environmental liabilities	195	70	265
Less: discounting accumulated liabilities to present value	23	3	26
Discounted environmental liabilities	172	67	239

At December 31, 2015, the estimated future environmental expenditures were as follows:

(millions of Canadian dollars)	
2016	22
2017	25
2018	26
2019	28
2020	30
Thereafter	98
	229

Hydro One records a liability for the estimated future expenditures for land assessment and remediation and for the phase-out and destruction of PCB-contaminated mineral oil removed from electrical equipment when it is determined that future environmental remediation expenditures are probable under existing statute or regulation and the amount of the future expenditures can be reasonably estimated.

There are uncertainties in estimating future environmental costs due to potential external events such as changes in legislation or regulations, and advances in remediation technologies. In determining the amounts to be recorded as environmental liabilities, the Company estimates the current cost of completing required work and makes assumptions as to when the future expenditures will actually be

incurred, in order to generate future cash flow information. A long-term inflation rate assumption of approximately 2% has been used to express these current cost estimates as estimated future expenditures. Future expenditures have been discounted using factors ranging from approximately 2.0% to 6.3%, depending on the appropriate rate for the period when expenditures are expected to be incurred. All factors used in estimating the Company's environmental liabilities represent management's best estimates of the present value of costs required to meet existing legislation or regulations. However, it is reasonably possible that numbers or volumes of contaminated assets, cost estimates to perform work, inflation assumptions and the assumed pattern of annual cash flows may differ significantly from the Company's current assumptions. In addition, with respect to the PCB environmental liability, the availability of critical resources such as skilled labour and replacement assets and the ability to take maintenance outages in critical facilities may influence the timing of expenditures.

PCBs

The Environment Canada regulations, enacted under the *Canadian Environmental Protection Act, 1999*, govern the management, storage and disposal of PCBs based on certain criteria, including type of equipment, in-use status, and PCB-contamination thresholds. Under current regulations, Hydro One's PCBs have to be disposed of by the end of 2025, with the exception of specifically exempted equipment. Contaminated equipment will generally be replaced, or will be decontaminated by removing PCB-contaminated insulating oil and retro filling with replacement oil that contains PCBs in concentrations of less than 2 ppm.

The Company's best estimate of the total estimated future expenditures to comply with current PCB regulations is $168 million (2014 – $195 million). These expenditures are expected to be incurred over the period from 2016 to 2025. As a result of its annual review of environmental liabilities, the Company recorded a revaluation adjustment in 2015 to reduce the PCB environmental liability by $24 million (2014 – $33 million).

Land Assessment and Remediation

The Company's best estimate of the total estimated future expenditures to complete its land assessment and remediation program is $61 million (2014 – $70 million). These expenditures are expected to be incurred over the period from 2016 to 2023. As a result of its annual review of environmental liabilities, the Company recorded a revaluation adjustment in 2015 to increase the land assessment and remediation environmental liability by $1 million (2014 – $13 million).

17. Asset Retirement Obligations

Hydro One records a liability for the estimated future expenditures for the removal and disposal of asbestos-containing materials installed in some of its facilities and for the decommissioning of specific switching stations located on unowned sites. Asset retirement obligations, which represent legal obligations associated with the retirement of certain tangible long-lived assets, are computed as the present value of the projected expenditures for the future retirement of specific assets and are recognized in the period in which the liability is incurred, if a reasonable estimate of fair value can be made. If the asset remains in service at the recognition date, the present value of the liability is added to the carrying amount of the associated asset in the period the liability is incurred and this additional carrying amount is depreciated over the remaining life of the asset. If an asset retirement obligation is recorded in respect of an out-of-service asset, the asset retirement cost is charged to results of operations. Subsequent to the initial recognition, the liability is adjusted for any revisions to the estimated future cash flows associated with the asset retirement obligation, which can occur due to a number of factors including, but not limited to, cost escalation, changes in technology applicable to the assets to be retired, changes in legislation or regulations, as well as for accretion of the liability due to the passage of time until the obligation is settled. Depreciation expense is adjusted prospectively for any increases or decreases to the carrying amount of the associated asset.

In determining the amounts to be recorded as asset retirement obligations, the Company estimates the current fair value for completing required work and makes assumptions as to when the future expenditures will actually be incurred, in order to generate future cash flow information. A long-term inflation assumption of approximately 2% has been used to express these current cost estimates as estimated future expenditures. Future expenditures have been discounted using factors ranging from approximately 3.0% to 5.0%, depending on the appropriate rate for the period when expenditures are expected to be incurred. All factors used in estimating the Company's asset retirement obligations represent management's best estimates of the cost required to meet existing legislation or regulations. However, it is reasonably possible that numbers or volumes of contaminated assets, cost estimates to perform work, inflation assumptions and the assumed pattern of annual cash flows may differ significantly from the Company's current assumptions. Asset retirement obligations are reviewed annually or more frequently if significant changes in regulations or other relevant factors occur. Estimate changes are accounted for prospectively.

At December 31, 2015, Hydro One had recorded asset retirement obligations of $9 million (2014 – $9 million), consisting of $8 million (2014 – $8 million) related to the estimated future expenditures associated with the removal and disposal of asbestos-containing

materials installed in some of its facilities, as well as $1 million (2014 – $1 million) related to the future decommissioning and removal of two switching stations. The amount of interest recorded is nominal.

18. Share Capital

Common Shares

The Company is authorized to issue an unlimited number of common shares. At December 31, 2015, the Company had 595,000,000 common shares issued and outstanding.

The amount and timing of any dividends payable by Hydro One is at the discretion of the Hydro One Board of Directors and is established on the basis of Hydro One's results of operations, maintenance of its deemed regulatory capital structure, financial condition, cash requirements, the satisfaction of solvency tests imposed by corporate laws for the declaration and payment of dividends and other factors that the Board of Directors may consider relevant.

Preferred Shares

The Company is authorized to issue an unlimited number of preferred shares, issuable in series. At December 31, 2015, two series of preferred shares are authorized for issuance: the Series 1 preferred shares and the Series 2 preferred shares. At December 31, 2015, the Company had 16,720,000 Series 1 preferred shares and no Series 2 preferred shares issued and outstanding.

Hydro One may from time to time issue preferred shares in one or more series. Prior to issuing shares in a series, the Hydro One Board of Directors is required to fix the number of shares in the series and determine the designation, rights, privileges, restrictions and conditions attaching to that series of preferred shares. Holders of Hydro One's preferred shares are not entitled to receive notice of, to attend or to vote at any meeting of the shareholders of Hydro One except that votes may be granted to a series of preferred shares when dividends have not been paid on any one or more series as determined by the applicable series provisions. Each series of preferred shares ranks on parity with every other series of preferred shares, and are entitled to a preference over the common shares and any other shares ranking junior to the preferred shares, with respect to dividends and the distribution of assets and return of capital in the event of the liquidation, dissolution or winding up of Hydro One.

For the period commencing from the date of issue of the Series 1 preferred shares and ending on and including November 19, 2020, the holders of Series 1 preferred shares are entitled to receive fixed cumulative preferential dividends of $1.0625 per share per year, if and when declared by the Board of Directors, payable quarterly. The dividend rate will reset on November 20, 2020 and every five years thereafter at a rate equal to the sum of the then five year Government of Canada bond yield and 3.53%. The Series 1 preferred shares will not be redeemable by Hydro One prior to November 20, 2020, but will be redeemable by Hydro One on November 20, 2020 and on November 20 of every fifth year thereafter at a redemption price equal to $25.00 for each Series 1 preferred share redeemed, plus any accrued or unpaid dividends. The holders of Series 1 preferred shares will have the right, at their option, on November 20, 2020 and on November 20 of every fifth year thereafter, to convert all or any of their Series 1 preferred shares into Series 2 preferred shares on a one-for-one basis, subject to certain restrictions on conversion. At December 31, 2015, Series 1 preferred dividends of $3 million or $0.18 per share were in arrears.

The holders of Series 2 preferred shares will be entitled to receive quarterly floating rate cumulative dividends, if and when declared by the Board of Directors, at a rate equal to the sum of the then three month Government of Canada treasury bill rate and 3.53% as reset quarterly. The Series 2 preferred shares will not be redeemable by Hydro One prior to November 20, 2020, but will be redeemable by Hydro One at a redemption price equal to $25.00 for each Series 2 preferred share redeemed, if redeemed on November 20, 2025 or on November 20 of every fifth year thereafter, or $25.50 for each Series 2 preferred share redeemed, if redeemed on any other date after November 20, 2020, in each case plus any accrued or unpaid dividends. The holders of Series 2 preferred shares will have the right, at their option, on November 20, 2025 and on November 20 of every fifth year thereafter, to convert all or any of their Series 2 preferred shares into Series 1 preferred shares on a one-for-one basis, subject to certain restrictions on conversion.

Prior to October 31, 2015, the Company had 12,920,000 issued and outstanding 5.5% cumulative preferred shares held by the Province, with a redemption value of $25 per share or $323 million total value. These preferred shares were entitled to an annual cumulative dividend of $18 million, or $1.375 per share, which was payable on a quarterly basis. These preferred shares had conditions for their redemption that were outside the control of the Company because the Province could exercise its right to redeem in the event of change in ownership without approval of the Company's Board of Directors. At December 31, 2014, these preferred shares were classified on the Consolidated Balance Sheet as temporary equity because the redemption feature was outside the control of the Company. On October 31, 2015, these preferred shares were purchased and cancelled by Hydro One Inc. See "Reorganization" below for further details.

Reorganization

Prior to the completion of the IPO, Hydro One and Hydro One Inc. completed a series of transactions (Pre-IPO Transactions) that resulted in, among other things, on October 31, 2015, Hydro One acquiring all of the issued and outstanding shares of Hydro One Inc. from the Province and issuing new common shares and preferred shares to the Province.

The following tables present the changes to common and preferred shares as a result of Pre-IPO Transactions, as well as the movement in the number of common and preferred shares during the year ended December 31, 2015. There was no movement in common or preferred shares during the year ended December 31, 2014.

		Preferred Shares	
(millions of Canadian dollars)	Common Shares	Equity	Temporary Equity
Common shares issued – purchase and cancellation of preferred shares *(c)*	323	–	(323)
Acquisition of Hydro One Inc. *(d)*			
Common shares of Hydro One Inc. acquired by Hydro One	(3,441)	–	–
Common shares of Hydro One issued to Province	3,023	–	–
Preferred shares of Hydro One issued to Province	–	418	–
Common shares issued *(e)*	2,600	–	–
Total Pre-IPO Transactions adjustment	2,505	418	(323)

		Preferred Shares	
(number of shares)	Common Shares	Equity	Temporary Equity
Number of shares – January 1, 2015 *(a)*	100,000	–	12,920,000
Common shares issued *(b)*	100,000	–	–
Pre-IPO Transactions:			
Common shares issued – purchase and cancellation of preferred shares *(c)*	2,640	–	(12,920,000)
Acquisition of Hydro One Inc.*(d)*			
Common shares of Hydro One Inc. acquired by Hydro One	(102,640)	–	–
Common shares of Hydro One issued to Province	12,197,500,000	–	–
Preferred shares of Hydro One issued to Province	–	16,720,000	–
Common shares issued *(e)*	2,600,000,000	–	–
Common shares consolidation *(f)*	(14,202,600,000)	–	–
Number of shares – December 31, 2015	595,000,000	16,720,000	–

(a) At January 1, 2015, all common and preferred shares represent the shares of Hydro One Inc.

(b) On August 31, 2015, Hydro One was incorporated under the *Business Corporations Act* (Ontario) and issued 100,000 common shares to the Province for proceeds of $100,000.

(c) On October 31, 2015, Hydro One Inc. purchased and cancelled 12,920,000 preferred shares of Hydro One Inc. previously held by the Province for cancellation at a price equal to the redemption price of the preferred shares totaling $323 million, which was satisfied by the issuance to the Province of 2,640 common shares of Hydro One Inc.

(d) On October 31, 2015, all of the issued and outstanding common shares of Hydro One Inc. were acquired by Hydro One from the Province in return for 12,197,500,000 common shares of Hydro One and 16,720,000 Series 1 preferred shares of Hydro One.

(e) On November 4, 2015, Hydro One issued 2.6 billion common shares to the Province for proceeds of $2.6 billion.

(f) On November 4, 2015, the common shares of Hydro One were consolidated by way of articles of amendment approved by the Province as sole shareholder so that, after such consolidation, 595,000,000 common shares of Hydro One were issued and outstanding.

Share Ownership Restrictions

The *Electricity Act* imposes share ownership restrictions on securities of Hydro One carrying a voting right (Voting Securities). These restrictions provide that no person or company (or combination of persons or companies acting jointly or in concert) may beneficially own or exercise control or direction over more than 10% of any class or series of Voting Securities, including common shares of the Company (Share Ownership Restrictions). The Share Ownership Restrictions do not apply to Voting Securities held by the Province, nor to an underwriter who holds Voting Securities solely for the purpose of distributing those securities to purchasers who comply with the Share Ownership Restrictions.

19. Dividends

In 2015, preferred share dividends in the amount of $13 million (2014 – $18 million) and common share dividends in the amount of $875 million (2014 – $269 million) were declared.

In August 2015, Hydro One declared a dividend in kind on its common shares payable in all of the issued and outstanding shares of Hydro One Brampton. See Note 4 – Business Combinations.

20. Earnings Per Share

Basic earnings per common share (EPS) is calculated by dividing net income attributable to common shareholders of Hydro One by the weighted average number of common shares outstanding.

Diluted EPS is calculated by dividing net income attributable to common shareholders of Hydro One by the weighted average number of common shares outstanding adjusted for the effects of potentially dilutive share grant plans, which is calculated using the treasury stock method.

Year ended December 31	2015	2014
Net income attributable to common shareholders *(millions of Canadian dollars)*	690	731
Weighted average number of shares		
Basic	496,272,733	477,837,100
Effect of dilutive share grant plans *(Note 21)*	94,691	
Diluted	496,367,424	477,837,100
EPS		
Basic	$1.39	$1.53
Diluted	$1.39	$1.53

Pro forma Adjusted non-GAAP Basic and Diluted EPS

The following pro forma adjusted non-GAAP basic and diluted EPS has been prepared by management on a supplementary basis which assumes that the total number of common shares outstanding was 595,000,000 in each of the years ended December 31, 2015 and 2014. The supplementary pro forma disclosure is used internally by management subsequent to the IPO of Hydro One to assess the Company's performance and is considered useful because it eliminates the impact of the issuance of common shares to the Province prior to the IPO. Prior to the IPO, the Province was the sole shareholder of Hydro One and disclosure of EPS did not provide meaningful information. EPS is considered an important measure and management believes that presenting it for all periods based on the number of outstanding shares on, and subsequent to, the IPO provides users with a basis to evaluate the operations of the Company with comparable companies.

Year ended December 31 *(unaudited)*	2015	2014
Net income attributable to common shareholders *(millions of Canadian dollars)*	690	731
Pro forma weighted average number of common shares		
Basic	595,000,000	595,000,000
Effect of dilutive share grant plans *(Note 21)*	94,691	
Diluted	595,094,691	595,000,000
Pro forma adjusted non-GAAP EPS		
Basic	$1.16	$1.23
Diluted	$1.16	$1.23

The above pro forma adjusted non-GAAP basic and diluted EPS does not have any standardized meaning in US GAAP.

21. Stock-based Compensation

Share Grant Plans

At December 31, 2015, Hydro One had two share grant plans, one for the benefit of certain members of the Power Workers' Union (the PWU Share Grant Plan) and one for the benefit of certain members of The Society of Energy Professionals (the Society Share Grant Plan).

The PWU Share Grant Plan provides for the issuance of common shares of Hydro One from treasury to certain eligible members of the Power Workers' Union annually, commencing on April 1, 2017 and continuing until the earlier of April 1, 2028 or the date an eligible employee no longer meets the eligibility criteria of the PWU Share Grant Plan. To be eligible, an employee must be a member of the Pension Plan on April 1, 2015, be employed on the date annual share issuance occurs and continue to have under 35 years of service. The requisite service period for the PWU share grant plan begins on July 3, 2015, which is the date the share grant plans were ratified by the PWU. The number of common shares issued annually to each eligible employee will be equal to 2.7% of such eligible employee's salary as at April 1, 2015, divided by $20.50, being the price of the common shares of Hydro One in the IPO. The aggregate number of common shares issuable under the PWU Share Grant Plan shall not exceed 3,981,763 common shares. In 2015, 3,979,062 common shares were granted under the PWU Share Grant Plan.

The Society Share Grant Plan provides for the issuance of common shares of Hydro One from treasury to certain eligible members of The Society of Energy Professionals annually, commencing on April 1, 2018 and continuing until the earlier of April 1, 2029 or the date an eligible employee no longer meets the eligibility criteria of the Society Share Grant Plan. To be eligible, an employee must be a member of the Pension Plan on September 1, 2015, be employed on the date annual share issuance occurs and continue to have under 35 years of service. Therefore the requisite service period for the Society Share Grant Plan begins on September 1, 2015. The number of common shares issued annually to each eligible employee will be equal to 2.0% of such eligible employee's salary as at September 1, 2015, divided by $20.50, being the price of the common shares of Hydro One in the IPO. The aggregate number of common shares issuable under the Society Share Grant Plan shall not exceed 1,434,686 common shares. In 2015, 1,433,292 common shares were granted under the Society Share Grant Plan.

The fair value of the share grants is estimated based on the grant date share price of $20.50 and is recognized using the graded vesting attribution method as the share grant plans have both a performance condition and a service condition. Total fair value of shares granted in 2015 is $111 million (2014 – $nil). Total share based compensation recognized during 2015 was $10 million (2014 – $nil) and was recorded as a regulatory asset. The historical turnover rate relating to members of the Power Workers' Union and The Society of Energy Professionals is not believed to be reflective of a future turnover rate due to benefits conferred by the share grant plans. At December 31, 2015 the Company expects all eligible employees to receive the share grants until such time that they no longer meet the eligibility criteria and therefore, a forfeiture rate of 0% is assumed in amounts recognized during 2015. The Company will reevaluate this assumption in subsequent periods based on actual experience.

A summary of share grant activity under the Plan as of December 31, 2015 is presented below:

Years ended December 31, 2015	Share Grants *(Number)*	Weighted-Average Price
Outstanding – beginning of year	–	–
Granted (non-vested)	5,412,354	$20.50
Outstanding – end of year	5,412,354	

Directors' DSU Plan

Under the Company's Directors' DSU Plan, directors can elect to receive credit for their annual cash retainer in a notional account of DSUs in lieu of cash. Hydro One's Board of Directors may also determine from time to time that special circumstances exist that would reasonably justify the grant of DSUs to a director as compensation in addition to any regular retainer or fee to which the director is entitled.

Each DSU represents a unit with an underlying value equivalent to the value of one common share of the Company and is entitled to accrue common share dividend equivalents in the form of additional DSUs at the time dividends are paid, subsequent to declaration by Hydro One's Board of Directors.

(number of DSUs)	2015	2014
DSUs outstanding – January 1	–	–
DSUs granted	20,525	–
DSUs outstanding – December 31	20,525	–

For the year ended December 31, 2015, an expense of less than $1 million (2014 – $nil) was recognized in earnings with respect to the DSU Plan. At December 31, 2015, a liability of less than $1 million (December 31, 2014 – $nil), related to outstanding DSUs has been recorded at the closing price of the Company's common shares of $22.29 and is included in accrued liabilities on the Balance Sheet.

Employee Share Ownership Plan

Effective December 15, 2015, Hydro One established an Employee Share Ownership Plan (ESOP). Under the ESOP, certain eligible management and non-represented employees may contribute between 1% and 6% of their base salary towards purchasing common shares of Hydro One. The Company will match 50% of the employee's contributions, up to a maximum Company contribution of $25,000 per calendar year. No contributions were made under the ESOP during 2015.

Long-term Incentive Plan

Effective August 31, 2015, the Board of Directors of Hydro One adopted a long-term Incentive Plan (LTIP). Under the LTIP, long-term incentives will be granted to certain executive and management employees, and all equity-based awards will be settled in newly issued shares of Hydro One from treasury, consistent with the provisions of the plan. The aggregate number of shares issuable under the LTIP shall not exceed 11,900,000 shares.

The LTIP provides flexibility to award a range of vehicles, including restricted share units, performance share units, stock options, share appreciation rights, restricted shares, deferred share units and other share-based awards. The mix of vehicles is intended to vary by role to recognize the level of executive accountability for overall business performance. No long-term incentives were awarded during 2015.

22. Noncontrolling Interest

On December 16, 2014, the relevant Bruce to Milton line transmission assets totalling $526 million were transferred from Hydro One Networks to B2M LP. This was financed by 60% debt ($316 million) and 40% equity ($210 million). On December 17, 2014, the Saugeen Ojibway Nation (SON) acquired a 34.2% equity interest in B2M LP for consideration of $72 million, representing the fair value of the equity interest acquired. The SON's initial investment in B2M LP consists of $50 million of Class A units and $22 million of Class B units.

The Class B units have a mandatory put option which requires that upon the occurrence of an enforcement event (i.e. an event of default such as a debt default by the SON or insolvency event), Hydro One purchase the Class B units of B2M LP for net book value on the redemption date. The noncontrolling interest relating to the Class B units is classified on the Consolidated Balance Sheet as temporary equity because the redemption feature is outside the control of the Company. The balance of the noncontrolling interest is classified within equity.

The following tables show the movements in noncontrolling interest for the years ended December 31, 2015 and December 31, 2014:

Year ended December 31, 2015 *(millions of Canadian dollars)*	Temporary Equity	Equity	Total
Noncontrolling interest – January 1, 2015	21	49	70
Distributions to noncontrolling interest	(1)	(4)	(5)
Net income attributable to noncontrolling interest	3	7	10
Noncontrolling interest – December 31, 2015	23	52	75

Year ended December 31, 2014 *(millions of Canadian dollars)*	Temporary Equity	Equity	Total
Noncontrolling interest – January 1, 2014	–	–	–
Amount contributed by noncontrolling interest	22	50	72
Net income (loss) attributable to noncontrolling interest	(1)	(1)	(2)
Noncontrolling interest – December 31, 2014	21	49	70

23. Related Party Transactions

The Province is the majority shareholder of Hydro One. The OEFC, IESO, Ontario Power Generation Inc. (OPG), the OEB, and Hydro One Brampton are related parties to Hydro One because they are controlled or significantly influenced by the Province. Effective January 1, 2015, the OPA and IESO have merged and are now operating as IESO.

The Province

- During 2015, Hydro One paid dividends to the Province totalling $888 million (2014 – $287 million). In addition, on August 31, 2015, Hydro One declared a dividend in-kind on its common shares payable in all of the issued and outstanding shares of Hydro One Brampton. See Note 4 – Business Combinations.
- On November 4, 2015, Hydro One issued common shares to the Province for proceeds of $2.6 billion. See Note 18 – Share Capital.
- During 2015, Hydro One Inc. incurred certain IPO related expenses totaling $7 million, which will be reimbursed to the Company by the Province.

IESO

- In 2015, Hydro One purchased power in the amount of $2,318 million (2014 – $2,601 million) from the IESO-administered electricity market.
- Hydro One receives revenues for transmission services from the IESO, based on OEB-approved uniform transmission rates. Transmission revenues for 2015 include $1,548 million (2014 – $1,556 million) related to these services.
- Hydro One receives amounts for rural rate protection from the IESO. Distribution revenues for 2015 include $127 million (2014 – $127 million) related to this program.
- Hydro One also receives revenues related to the supply of electricity to remote northern communities from the IESO. Distribution revenues for 2015 include $32 million (2014 – $32 million) related to these services.
- The IESO (OPA prior to January 1, 2015) funds substantially all of the Company's CDM programs. The funding includes program costs, incentives, and management fees. During 2015, Hydro One received $70 million (2014 – $33 million) related to these programs.

OPG

- In 2015, Hydro One purchased power in the amount of $11 million (2014 – $23 million) from OPG.
- Hydro One has service level agreements with OPG. These services include field, engineering, logistics and telecommunications services. In 2015, revenues related to the provision of construction and equipment maintenance services with respect to these service level agreements were $7 million (2014 – $12 million), primarily for the Transmission Business. Operation, maintenance and administration costs in 2015 and 2014 related to the purchase of services with respect to these service level agreements were not significant.

OEFC

- In 2015, Hydro One made PILs to the OEFC totalling $2.9 billion (2014 – $86 million), including Departure Tax of $2.6 billion (2014 – $nil).
- In 2015, Hydro One purchased power in the amount of $6 million (2014 – $9 million) from power contracts administered by the OEFC.
- During 2015, Hydro One paid a $8 million (2014 – $5 million) fee to the OEFC for indemnification against adverse claims in excess of $10 million paid by the OEFC with respect to certain of Ontario Hydro's businesses transferred to Hydro One on April 1, 1999. Hydro One has not made any claims under the indemnity since it was put in place in 1999. Hydro One and the OEFC, with the consent of the Minister of Finance, terminated the indemnity fee effective October 31, 2015.
- PILs and payments in lieu of property taxes were paid to the OEFC.

OEB

- Under the *Ontario Energy Board Act, 1998*, the OEB is required to recover all of its annual operating costs from gas and electricity distributors and transmitters. In 2015, Hydro One incurred $12 million (2014 – $12 million) in OEB fees.

Hydro One Brampton

- Effective August 31, 2015, Hydro One Brampton is no longer a subsidiary of Hydro One, but is indirectly owned by the Province. For change in ownership of Hydro One Brampton, see Note 4 – Business Combinations.
- Subsequent to August 31, 2015, Hydro One continues to provide certain management, administrative and smart meter network services to Hydro One Brampton pursuant to certain service level agreements, which are provided at market rates. These agreements will continue until the end of 2016 (except in the case of smart meter network services, which will continue until the end of 2017). Hydro One Brampton has the right to renew these agreements (other than smart meter network services) for additional one-year terms to end no later than December 31, 2019. Additionally, on August 31, 2015, Hydro One Inc. and Hydro One Brampton entered into a license agreement which permits Hydro One Brampton to use the "Hydro One" name and related licensed marks. These agreements will terminate if the Province disposes of its interest in Hydro One Brampton, except in the case of the smart meter network services agreement, which is anticipated to continue for a transition period after the Province disposes of its interest in Hydro One Brampton. During 2015, revenues related to the provision of services with respect to these service level agreements were $1 million.

Sales to and purchases from related parties occur at normal market prices or at a proxy for fair value based on the requirements of the OEB's Affiliate Relationships Code. Outstanding balances at period end are interest free and settled in cash.

The amounts due to and from related parties as a result of the transactions referred to above are as follows:

(millions of Canadian dollars)	**December 31, 2015**	December 31, 2014
Due from related parties	**191**	224
Due to related parties[1]	**(138)**	(227)

[1] Included in due to related parties at December 31, 2015 are amounts owing to the IESO in respect of power purchases of $134 million (2014 – $214 million).

24. Consolidated Statements of Cash Flows

The changes in non-cash balances related to operations consist of the following:

Year ended December 31

(millions of Canadian dollars)	**2015**	2014
Accounts receivable	**240**	(93)
Due from related parties	**33**	(27)
Materials and supplies	**2**	–
Prepaid expenses and other assets	**4**	(13)
Accounts payable	**(23)**	39
Accrued liabilities	**(15)**	(35)
Due to related parties	**(89)**	(3)
Accrued interest	**(4)**	–
Long-term accounts payable and other liabilities	**–**	(3)
Post-retirement and post-employment benefit liability	**60**	80
	208	(55)

Capital Expenditures

The following table illustrates the reconciliation between investments in property, plant and equipment and the amount presented in the Consolidated Statements of Cash Flows after accounting for capitalized depreciation and the net change in related accruals:

Year ended December 31 *(millions of Canadian dollars)*	2015	2014
Capital investments in property, plant and equipment	(1,623)	(1,511)
Capitalized depreciation and net change in accruals included in capital investments in property, plant and equipment	28	30
Capital expenditures – property, plant and equipment	(1,595)	(1,481)

The following table illustrates the reconciliation between investments in intangible assets and the amount presented in the Consolidated Statements of Cash Flows after accounting for the net change in related accruals:

Year ended December 31 *(millions of Canadian dollars)*	2015	2014
Capital investments in intangible assets	(40)	(19)
Net change in accruals included in capital investments in intangible assets	3	(4)
Capital expenditures – intangible assets	(37)	(23)

Capital Contributions

Hydro One enters into contracts governed by the OEB Transmission System Code when a transmission customer requests a new or upgraded transmission connection. The customer is required to make a capital contribution to Hydro One based on the shortfall between the present value of the costs of the connection facility and the present value of revenues. The present value of revenues is based on an estimate of load forecast for the period of the contract with Hydro One. Once the connection facility is commissioned, in accordance with the OEB Transmission System Code, Hydro One will periodically reassess the estimated of load forecast which will lead to a decrease, or an increase in the capital contributions from the customer. The increase or decrease in capital contributions is recorded directly to fixed assets in service. In 2015, capital contributions from these reassessments totalled $62 million, which represents the difference between the revised load forecast of electricity transmitted compared to the load forecast in the original contract, subject to certain adjustments. No reassessments occurred in 2014.

Supplementary Information

Year ended December 31 *(millions of Canadian dollars)*	2015	2014
Net interest paid	416	412
Income taxes / PILs paid	2,933	86

25. Contingencies

Legal Proceedings

Hydro One is involved in various lawsuits, claims and regulatory proceedings in the normal course of business. In the opinion of management, the outcome of such matters will not have a material adverse effect on the Company's consolidated financial position, results of operations or cash flows.

In September 2015, Hydro One and three of its subsidiaries were served with a class action suit in which the representative plaintiff is seeking up to $125 million in damages related to allegations of improper billing practices. Hydro One intends to defend the action. Due to the preliminary stage of legal proceedings, an estimate of a possible loss related to this claim cannot be made.

Transfer of Assets

The transfer orders by which the Company acquired certain of Ontario Hydro's businesses as of April 1, 1999 did not transfer title to some assets located on Reserves (as defined in the *Indian Act* (Canada)). Currently, the OEFC holds these assets. Under the terms of the transfer orders, the Company is required to manage these assets until it has obtained all consents necessary to complete the transfer of title of these assets to itself. The Company cannot predict the aggregate amount that it may have to pay, either on an annual or one-time basis, to obtain the required consents. In 2015, the Company paid approximately $1 million (2014 – $1 million) in respect of consents obtained. If the Company cannot obtain the required consents, the OEFC will continue to hold these assets for an indefinite period of time. If the Company cannot reach a satisfactory settlement, it may have to relocate these assets to other locations at a cost that could be substantial or, in a limited number of cases, to abandon a line and replace it with diesel-generation facilities. The costs relating to these assets could have a material adverse effect on the Company's results of operations if the Company is not able to recover them in future rate orders.

26. Commitments

Outsourcing Agreements

Inergi LP (Inergi), an affiliate of Capgemini Canada Inc., provides services to Hydro One, including settlements, source to pay services, pay operations services, information technology, finance and accounting services. The agreement with Inergi for these services expires in December 2019. In addition, Inergi provides customer service operations outsourcing services to Hydro One. The agreement for these services expires in February 2018.

Brookfield Global Integrated Solutions (formerly Brookfield Johnson Controls Canada LP) (Brookfield) provides services to Hydro One, including facilities management and execution of certain capital projects as deemed required by the Company. The current agreement with Brookfield expires in December 2024.

At December 31, 2015, the annual commitments under the outsourcing agreements were as follows: 2016 – $167 million; 2017 – $138 million; 2018 – $106 million; 2019 – $99 million; 2020 – $2 million; and thereafter – $11 million.

Trilliant Agreement

In December 2015, Hydro One entered into an agreement with Trilliant Holdings Inc. and Trilliant Networks (Canada) Inc. (Trilliant) for the supply, maintenance and support services for smart meters and related hardware and software, including additional software licenses, as well as certain professional services. This agreement is for a term of ten years, from December 31, 2015 to December 31, 2025, with the option to renew for an additional term of five years at Hydro One's sole discretion. At December 31, 2015, the annual commitments under the agreement were as follows: 2016 – $17 million; 2017 – $17 million; 2018 – $17 million; 2019 – $17 million; 2020 – $16 million; and thereafter – $6 million.

Prudential Support

Purchasers of electricity in Ontario, through the IESO, are required to provide security to mitigate the risk of their default based on their expected activity in the market. As at December 31, 2015, Hydro One Inc. provided prudential support to the IESO on behalf of its subsidiaries using parental guarantees of $329 million (2014 – $330 million), and on behalf of a distributor using guarantees of $1 million (2014 – $1 million). In addition, as at December 31, 2015, Hydro One Inc. has provided letters of credit in the amount of $15 million (2014 – $8 million) to the IESO. The IESO could draw on these guarantees and/or letters of credit if these subsidiaries or distributor fail to make a payment required by a default notice issued by the IESO. The maximum potential payment is the face value of any letters of credit plus the amount of the parental guarantees.

Retirement Compensation Arrangements

Bank letters of credit have been issued to provide security for Hydro One Inc.'s liability under the terms of a trust fund established pursuant to the supplementary pension plan for eligible employees of Hydro One Inc. The supplementary pension plan trustee is required to draw upon these letters of credit if Hydro One Inc. is in default of its obligations under the terms of this plan. Such obligations include the requirement to provide the trustee with an annual actuarial report as well as letters of credit sufficient to secure Hydro One Inc.'s liability under the plan, to pay benefits payable under the plan and to pay the letter of credit fee. The maximum potential payment is the face value of the letters of credit. At December 31, 2015, Hydro One Inc. had letters of credit of $139 million (2014 – $126 million) outstanding relating to retirement compensation arrangements.

Operating Leases

Hydro One is committed as lessee to irrevocable operating lease contracts for buildings used in administrative and service-related functions and storing telecommunications equipment. These leases have typical terms of between three and five years, but several leases have lesser or greater terms to address special circumstances and/or opportunities. Renewal options, which are generally prevalent in most leases, have similar terms of three to five years. All leases include a clause to enable upward revision of the rental charge on an annual

basis or on renewal according to prevailing market conditions or pre-established rents. There are no restrictions placed upon Hydro One by entering into these leases.

During the year ended December 31, 2015, the Company made lease payments totaling $7 million (2014 – $11 million). At December 31, 2015, the future minimum lease payments under non-cancellable operating leases were as follows; 2016 – $11 million; 2017 – $10 million; 2018 – $9 million; 2019 – $4 million; 2020 – $8 million; and thereafter – $3 million.

27. Segmented Reporting

Hydro One has three reportable segments:

- The Transmission Business, which comprises the core business of transmitting high voltage electricity across the province, interconnecting more than 70 local distribution companies and certain large directly connected industrial customers throughout the Ontario electricity grid;
- The Distribution Business, which comprises the core business of delivering electricity to end customers and certain other municipal electricity distributors; and
- Other Business, which includes certain corporate activities and the operations of the Company's telecommunications business.

The designation of segments has been based on a combination of regulatory status and the nature of the products and services provided. Operating segments of the Company are determined based on information used by the chief operating decision maker in deciding how to allocate resources and evaluate the performance of each of the segments. The Company evaluates segment performance based on income before financing charges and income taxes from continuing operations (excluding certain allocated corporate governance costs).

The accounting policies followed by the segments are the same as those described in the summary of significant accounting policies (see Note 2 – Significant Accounting Policies). Segment information on the above basis is as follows:

Year ended December 31, 2015 *(millions of Canadian dollars)*	Transmission	Distribution	Other	Consolidated
Revenues	1,536	4,949	53	6,538
Purchased power	–	3,450	–	3,450
Operation, maintenance and administration	426	633	76	1,135
Depreciation and amortization	374	380	5	759
Income (loss) before financing charges and income taxes	736	486	(28)	1,194
Capital investments	943	711	9	1,663

Year ended December 31, 2014 *(millions of Canadian dollars)*	Transmission	Distribution	Other	Consolidated
Revenues	1,588	4,903	57	6,548
Purchased power	–	3,419	–	3,419
Operation, maintenance and administration	394	742	56	1,192
Depreciation and amortization	346	367	9	722
Income (loss) before financing charges and income taxes	848	375	(8)	1,215
Capital investments	845	680	5	1,530

Total Assets by Segment:

December 31 *(millions of Canadian dollars)*	2015	2014
Transmission	12,066	12,540
Distribution	9,213	9,805
Other	3,049	205
Total assets	24,328	22,550

All revenues, costs and assets, as the case may be, are earned, incurred or held in Canada.

28. Subsequent Events

Dividends

On February 11, 2016, preferred share dividends in the amount of $6 million and common share dividends in the amount of $202 million were declared.

Dividend Reinvestment Plan

On February 11, 2016, Hydro One's Board of Directors approved the creation of a Dividend Reinvestment Plan which the Company currently intends to put in place in March 2016. The Dividend Reinvestment Plan will enable eligible shareholders to have their regular quarterly cash dividends automatically reinvested in additional Hydro One common shares acquired on the open market.

Great Lakes Power Transmission Purchase Agreement

On January 28, 2016, Hydro One reached an agreement to acquire from Brookfield Infrastructure various entities that own and control Great Lakes Power Transmission LP, an Ontario regulated electricity transmission business operating along the eastern shore of Lake Superior, north and east of Sault Ste. Marie, Ontario, for $222 million in cash, subject to customary adjustments, plus the assumption of approximately $151 million in outstanding indebtedness. The acquisition is pending a *Competition Act* approval as well as regulatory approval from the OEB.

CORPORATE AND SHAREHOLDER INFORMATION

Corporate Address
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tel: 416-345-5000 or 1-877-955-1155
www.HydroOne.com

Customer Inquiries
Hydro One Networks Inc.
P.O. Box 5700
Markham, ON L3R 1C8

Billing and Service Inquiries:
tel: 1-888-664-9376
fax: 1-888-625-4401 or 905-944-3251
e-mail: CustomerCommunications@HydroOne.com

Report an Emergency (24 hours):
tel: 1-800-434-1235

General Shareholder Inquiries
Computershare Trust Company of Canada
100 University Avenue
Toronto, ON M5J 2Y1
tel: 514-982-7555 or 1-800-564-6253
fax: 1-888-453-0330 or 416-263-9394
e-mail: service@computershare.com

Dividend Reinvestment Plan (DRIP)
tel: 514-982-7555 or 1-800-564-6253
www.HydroOne.com/DRIP

Institutional Investors and Securities Analysts
tel: 416-345-6867
e-mail: investor.relations@HydroOne.com

Media Inquiries
tel: 416-345-6868 or 1-877-506-7584

Dividends
Unless indicated otherwise, all dividends paid by Hydro One Limited to common shareholders are designated as "eligible" dividends for the purpose of the Income Tax Act (Canada) and any similar provincial legislation.

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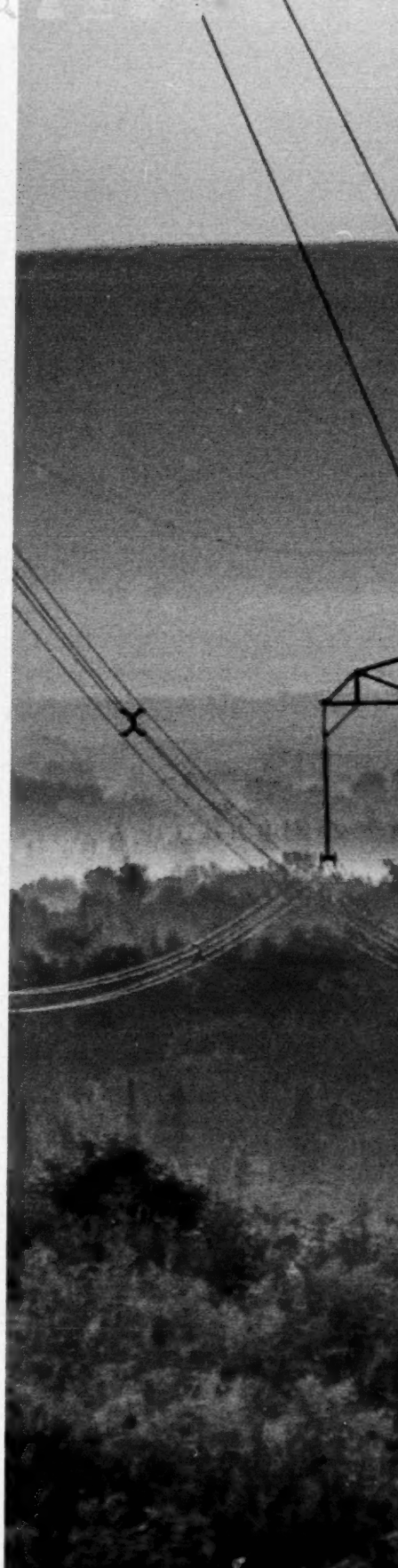

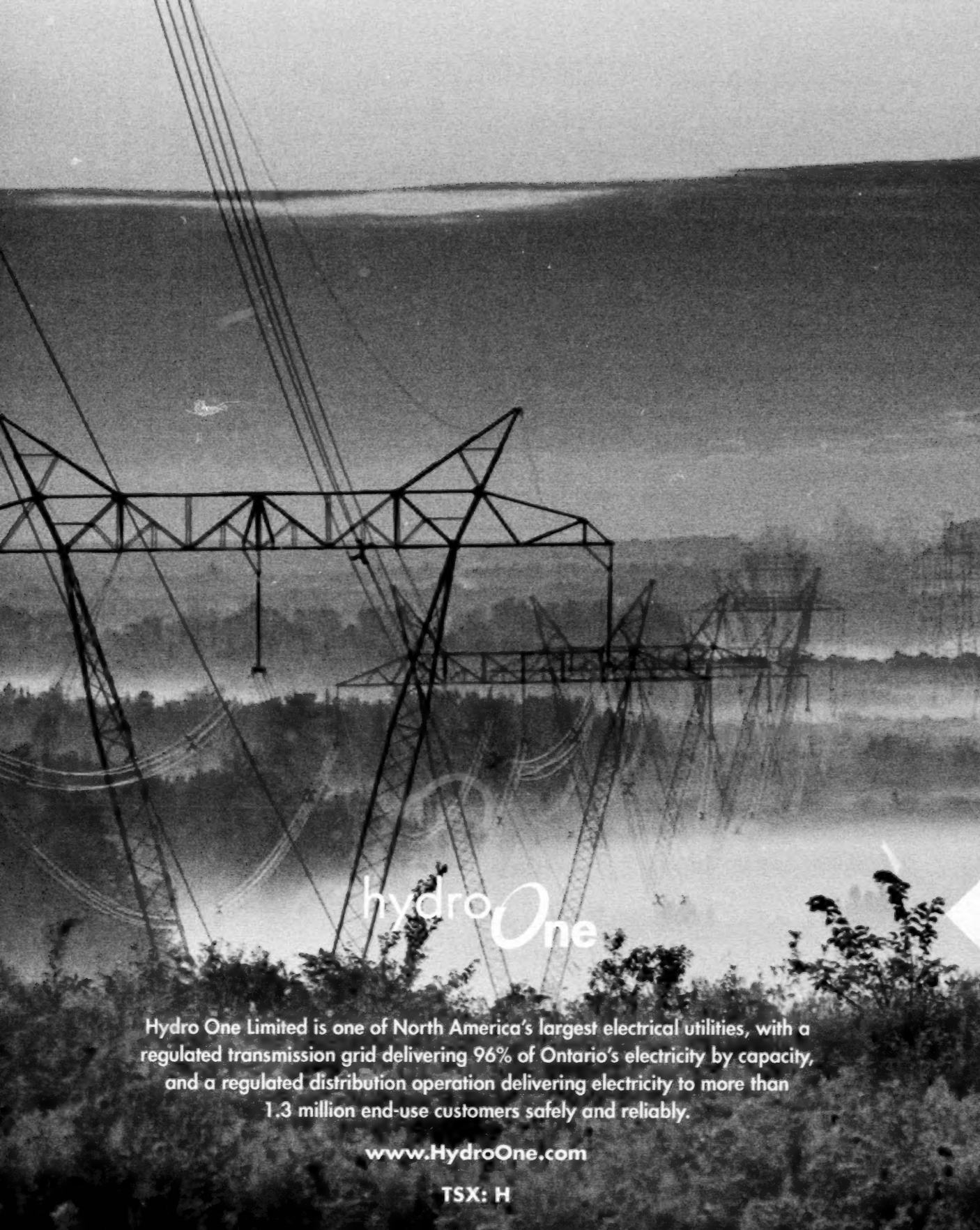

Hydro One Limited is one of North America's largest electrical utilities, with a regulated transmission grid delivering 96% of Ontario's electricity by capacity, and a regulated distribution operation delivering electricity to more than 1.3 million end-use customers safely and reliably.

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